

# FUNDING STRATEGY STATEMENT

## LONDON BOROUGH OF WALTHAM FOREST PENSION FUND

MARCH 2020

London Borough of Waltham Forest

This Funding Strategy Statement has been prepared by London Borough of Waltham Forest (the Administering Authority) to set out the funding strategy for the London Borough of Waltham Forest Pension Fund (the “Fund”), in accordance with Regulation 58 of the Local Government Pension Scheme Regulations 2013 (as amended) and guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA).

## EXECUTIVE SUMMARY

Ensuring that the London Borough of Waltham Forest Pension Fund (the “Fund”) has sufficient assets to meet its pension liabilities in the long term is the fiduciary responsibility of the Administering Authority (London Borough of Waltham Forest). The Funding Strategy adopted by the London Borough of Waltham Forest Pension Fund will therefore be critical in achieving this.

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

The details contained in this Funding Strategy Statement will have a financial and operational impact on all participating employers in the London Borough of Waltham Forest Pension Fund.

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

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

### THE FUND’S OBJECTIVE



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

However, because financial and market conditions/outlook change between valuations, the assumptions used at one valuation may need to be amended at the next to meet the primary objective. This in turn means that contributions will be subject to change from one valuation to another.

The objective is considered on an employer specific level where appropriate, including when setting individual contribution rates so each employer has the same fundamental objective in relation to their liabilities.

The general principle adopted by the Fund is that the assumptions used, taken as a whole, will be chosen sufficiently prudently for pensions already in payment to continue to be paid, and to reflect the commitments that will arise from members’ accrued pension rights.

The funding strategy set out in this document has been developed alongside the Fund’s investment strategy on an integrated basis, taking into account the overall financial and demographic risks inherent in the Fund to meet the objective for all employers over different periods. The funding strategy includes appropriate margins to allow for the possibility of adverse events (e.g. material reduction in investment returns, economic downturn and higher inflation outlook) leading to a worsening of the funding position which would normally lead to volatility of contribution rates at future valuations if these margins were not included.

This prudence is required by the Regulations and guidance issued by professional bodies and Government agencies to assist the Fund in meeting its primary solvency and long term cost efficiency objectives.



## SOLVENCY AND LONG TERM COST EFFICIENCY

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

Employer contributions are also set in order to achieve long term cost efficiency. Long term cost-efficiency implies that contributions must not be set at a level that is likely to give rise to additional costs in the future. For example, deferring costs to the future would be likely to result in those costs being greater overall than if they were provided for at the appropriate time. Equally, the FSS must have regard to the desirability of maintaining as nearly constant a primary rate of contribution as possible.

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

## DEFICIT RECOVERY PLAN AND CONTRIBUTIONS



As the solvency level of the Fund is 80% at the valuation date (i.e. the assets of the Fund are less than the liabilities), a deficit recovery plan needs to be implemented such that additional contributions are paid into the Fund to meet the shortfall.

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

The objective is to recover any deficit over a reasonable timeframe, and this will be periodically reviewed. Subject to affordability considerations a key principle will be to maintain the deficit contributions at least at the expected monetary levels from the preceding valuation (including any indexation in these monetary payments over the recovery period). Full details are set out in this FSS.

The target recovery period for the Fund as a whole is 19 years at this valuation, which is three years lower than the corresponding target recovery period from the previous valuation. Individual employer recovery periods will be considered depending on their own circumstances. Subject to affordability and other considerations, individual employer recovery periods would be expected to be a continuation of those set at the previous valuation. The average recovery period emerging from this valuation is 17 years.

Where there is a material increase in contributions required at this valuation, in certain circumstances the employer may be permitted to 'phase in' contribution increases over a period of up to 3 years in

a pattern agreed with the Administering Authority. Any such arrangement will be at the sole discretion of the Administering Authority depending on its view of the affordability of contributions (as assessed in a covenant review of the employer if necessary).

The Government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment. Therefore, the Fund has considered its policy in relation to costs that could emerge from the McCloud judgment in line with the guidance from the Scheme Advisory Board in conjunction with the Actuary. Whilst the remedy is not known and may not be known for some time, for the purpose of this valuation, when considering the appropriate contribution provision, we have assumed that the judgment would have the effect of removing the current age criteria applied to the underpin implemented in 2014 for the LGPS. This underpin therefore would apply to all active members as at 1 April 2012. The relevant estimated costs have been quantified and notified to employers on this basis but also highlighting that the final costs may be significantly different. All employers in the Fund as at 31 March 2019 have chosen to include these estimated costs over 2020/23 in their certified contributions.



## ACTUARIAL ASSUMPTIONS

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

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

The assumption for long term expected future real returns has reduced since the last valuation. This is due to a combination of a fall in the total expectation of the return on the Fund’s assets and the higher expected level of inflation in the long term. The Fund has also implemented risk management strategies since the last valuation that aim to reduce the expected volatility of returns (and therefore provide more certainty on contribution outcomes). Taking into account all of the above, the discount rate has been adjusted from the previous valuation so that, in the Actuary’s opinion, when allowing for the resultant employer contributions emerging from the valuation, the Fund can still reasonably be expected to meet the Solvency and Long Term Cost Efficiency objectives.

The Fund Actuary is proposing that the real discount rate assumption for determining the baseline past service liabilities should be 1.95% per annum, and for determining the future service (“primary”) contribution rate 2.5% per annum. This compares to 2.2% per annum and 2.75% per annum respectively at the last valuation.

Where warranted by an employer’s circumstances, the Administering Authority retains the discretion to apply a discount rate based on a lower risk investment strategy for that employer to protect the Fund as a whole. Such cases will be determined by the Section 151 Officer and reported to the Committee.

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

terminating participation in the Fund, a more prudent mortality assumption will apply (see further comments below).



## EMPLOYER ASSET SHARES

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

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

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



## FUND POLICIES

In addition to the information/approaches required by overarching guidance and Regulation, this statement also summarises the Fund's practice and policies in a number of key areas:

### 1. Covenant assessment and monitoring

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

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

After the valuation, the Fund may look to monitor employers' covenants in conjunction with their funding positions over the inter-valuation period. This will enable the Fund to anticipate and pre-empt any material issues arising and thus adopt a proactive approach in partnership with the employer.

### 2. Admitting employers to the Fund

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

- Mandatory Scheme Employers - for example new academies (see later section);
- Designated bodies - those that are permitted to join if they pass a resolution;
- Admission bodies - usually arising as a result of an outsourcing or a transfer to an entity that provides some form of public service and where the body's funding primarily derives from local or central government;

The key objective for the Fund is to only admit employers where the risk to the Fund is mitigated as far as possible. The different employers pose different risks to the Fund.

Certain employers may be required to provide a guarantee or alternative security before entry will be allowed, in accordance with the Regulations and Fund policies.

### 3. Termination policy for employers exiting the Fund

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

Where there is no guarantor who would subsume the liabilities of the exiting employer, the Fund's policy is that a discount rate linked to government bond yields and a more prudent longevity assumption will be used for assessing liabilities on termination. Any resulting exit payments due should normally be paid immediately, although instalment plans will be considered by the Administering Authority on a case by case basis. The Administering Authority also reserves the right to modify this approach on a case by case basis if circumstances warrant it.

Any exit credits (surplus assets over liabilities) will be paid from the Fund to the exiting employer within 6 months of completion of the cessation assessment by the Actuary. The Administering Authority may seek to modify this approach on a case by case basis if circumstances warrant it (for example, it may work with the outsourcing scheme employer to adjust any exit payment or exit credit to take into account any risk sharing arrangements which exist between the exiting employer and other Fund employers).

This is subject to the exiting employer providing sufficient notice to the Fund of their intent to exit; any delays in notification will impact on the payment date. The Administering Authority also reserves the right to modify this approach on a case by case basis if circumstances warrant it based on the advice of the Actuary.

Where there is a **guarantor** who would subsume the assets and liabilities of the outgoing employer, the default policy is that any deficit or surplus would be subsumed into the guarantor and taken into account at the following valuation. In some instances an exit debt may be payable by an employer before the assets and liabilities are subsumed by the guarantor, this will be considered on a case-by-case basis. No exit credit would be payable in these circumstances.

In line with the amending Regulations (The Local Government Pension Scheme (Amendment) Regulations 2020) the parties will need to make representations to the Administering Authority if they believe an exit credit should be paid outside the policy set out above, or if they dispute the determination of the Administering Authority. The Administering Authority will provide details of the information required to make their determination for each case when the need arises.

The Administering Authority can modify this approach on a case by case basis if circumstances warrant it and the parties make representation. For example if the parties make representation it may be appropriate to adjust any exit payment or exit credit to take into account any risk sharing arrangements which exist between the exiting employer and the outsourcing scheme employer.

In the event of parties unreasonably seeking to crystallise an exit credit on termination, the Fund will consider its overall policy and seek to recover termination deficits as opposed to allowing them to be

subsumed with no impact on contribution requirements until the next assessment of the contribution requirements for the guarantor. Equally where a guarantor decides not to underwrite the residual liabilities the basis of assessment on termination will assume the liabilities are orphaned and thus the minimum risk basis will apply.

#### **4. Academies Policy**

The Fund currently operates a policy whereby for the purpose of setting contribution rates, any new academies entering the Fund are pooled together with other academies (primarily those who converted on or after 1 July 2012) and also schools which remain under the control of the local education authority. Details on how this policy operates are set out in Appendix D.

## CONTENTS

Executive Summary .....	i
Introduction.....	8
Purpose of FSS in policy terms .....	10
Aims and purpose of the Fund .....	11
Responsibilities of the key parties .....	12
Solvency funding target .....	14
Link to investment policy and the Investment strategy statement (ISS).....	19
Identification of risks and counter-measures .....	21
Monitoring and review .....	24

## APPENDICES

A - ACTUARIAL METHOD AND ASSUMPTIONS

B - EMPLOYER DEFICIT RECOVERY PLANS

C - ADMISSION AND TERMINATION POLICY

D – ACADEMIES POLICY

E - GLOSSARY OF TERMS

# 1

## INTRODUCTION

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

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

### BENEFITS

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

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

### EMPLOYER CONTRIBUTIONS

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

## PRIMARY RATE

The “Primary rate” for an employer is the contribution rate required to meet the cost of the future accrual of benefits, ignoring any past service surplus or deficit, but allowing for any employer-specific circumstances, such as its membership profile, the funding strategy adopted for that employer, the actuarial method used and/or the employer’s covenant.

The Primary rate for each employer is specified in the rates and adjustments certificate.

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

## SECONDARY RATE

The “Secondary rate” is an adjustment to the Primary rate to arrive at the total rate of contribution each employer is required to pay. The Secondary rate may be expressed as a percentage adjustment to the Primary rate, and/or a cash adjustment in each of the three years beginning 1 April in the year following the actuarial valuation.

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

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

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

# 2

## PURPOSE OF FSS IN POLICY TERMS

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

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

The purpose of this Funding Strategy Statement is therefore:

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

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

# 3

## AIMS AND PURPOSE OF THE FUND

### THE AIMS OF THE FUND ARE TO:

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

### THE PURPOSE OF THE FUND IS TO:

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

# 4

## RESPONSIBILITIES OF THE KEY PARTIES

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

### KEY PARTIES TO THE FSS

The **Administering Authority** should:

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

The **Individual Employer** should:

- deduct contributions from employees' pay correctly after determining the appropriate employee contribution rate (in accordance with the Regulations);
- pay all contributions, including employer contributions as determined by the actuary, promptly by the due date;
- undertake such administration duties as are required in accordance with the Pension Administration Strategy (once implemented);

- develop a policy on certain discretions and exercise those discretions as permitted within the regulatory framework;
- make additional contributions as necessary in accordance with agreed arrangements in respect of, for example, augmentations of Fund benefits or early retirement strains;
- have regard to the Pensions Regulator's focus on data quality and comply with any requirement set by the Administering Authority in this context; and
- notify the Administering Authority promptly of any changes to membership which may affect future funding.

The **Fund Actuary** should:

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

# 5

## SOLVENCY FUNDING TARGET

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

### SOLVENCY AND LONG TERM EFFICIENCY

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

Employer contributions are also set in order to achieve long term cost efficiency. Long term cost-efficiency implies that contributions must not be set at a level that is likely to give rise to additional costs in the future. For example, deferring costs to the future would be likely to result in those costs being greater overall than if they were provided for at the appropriate time.

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

### DETERMINATION OF THE SOLVENCY FUNDING TARGET AND DEFICIT RECOVERY PLAN

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

Underlying these assumptions are the following two tenets:

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

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

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

As part of each valuation separate employer contribution rates are assessed by the Fund Actuary for each participating employer or group of employers. These rates are assessed taking into account the experience and circumstances of each employer, following a principle of no cross-subsidy between the distinct employers and employer groups in the Fund.

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

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

- the **Primary rate**: a percentage of pensionable payroll in respect of the cost of the future accrual of benefits and ancillary death in service and ill health benefits (where appropriate).
- the **Secondary rate**: a schedule of lump sum monetary amounts and/or % of pay amendment over 2020/23 in respect of an employer's surplus or deficit (which may be expressed as a % of payroll for certain employers) (including any phasing adjustments).

For any employer, the total contributions they are actually required to pay in any one year is the sum of the Primary and Secondary rates (subject to an overall minimum of zero). Both elements are subject to further review from 1 April 2023 based on the results of the 2022 actuarial valuation.

Where an employer is in a surplus position and a Secondary rate deduction applies (see comment below), the Secondary rate deduction from the Primary rate will be subject to a minimum annual threshold of £100, below which no deduction will be made.

#### DEFICIT RECOVERY PLAN

Where deficits remain, the Fund does not believe it to be appropriate for contribution reductions to apply compared to the existing funding plan (allowing for indexation where applicable on deficit contributions) unless there is a specific reason to do so.

Subject to consideration of affordability, as a general rule the deficit recovery period will have the same end date as the recovery period adopted at the preceding valuation. This is in order to target full solvency over a similar (or shorter) time horizon. Employers will have the freedom to adopt a recovery plan over a shorter period if they so wish. Taking into account affordability considerations and other factors, a bespoke period may be applied in respect of particular employers where the Administering Authority considers this to be warranted (see Deficit Recovery Plan in **Appendix B**). These principles have resulted in a maximum recovery period of 19 years being adopted for most Fund employers.

Where increases (or decreases) in employer contributions are required from 1 April 2020, following completion of the 2019 actuarial valuation, at the sole discretion of the Administering Authority the increase (or decrease) from the rates of contribution payable in the year 2020/21 may be implemented in steps, over a maximum period of 3 years.

For those employers assessed to be in surplus at the valuation date, the surplus will be removed over a maximum recovery period of 19 years, unless agreed otherwise with the Administering Authority.

For certain employers, subject to the agreement of the Administering Authority, the option to prepay contributions may be made available, with a discount applied to reflect the earlier payment date. This option may also be permitted for Primary rate contributions, but only on the proviso that a "top-up" payment would be made by the employer prior to the end of the prepayment period to reflect any

difference between actual and assumed pensionable payroll in order to ensure that no underpayment emerges versus the minimum required by the valuation certificate.

In all cases the Administering Authority reserves the right to apply a different approach at its sole discretion, taking into account the risk associated with an employer in proportion to the Fund as a whole (see further comment below). Any employer affected will be notified separately.

## EMPLOYERS EXITING THE FUND

Employers must notify the Fund as soon as they become aware of their planned exit date. Where appropriate, or at the request of the employer, the Fund will review the employer's certified contribution in order to target a fully funded position at exit. The costs of the contribution rate review will be payable by the employer or the outsourcing scheme employer (where necessary).

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

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

The residual assets and liabilities and hence any surplus or deficit will transfer back to the guarantor as a default policy

The interested parties will need to consider any separate agreements that have been put in place between the exiting employer and the guarantor. In some instances an exit credit or debt may be payable by an employer before the assets and liabilities are subsumed by the guarantor, this will be considered on a case-by-case basis.

If there is any dispute, then the following arrangements will apply:

- In the case of a surplus, in line with the amending Regulations ([The Local Government Pension Scheme \(Amendment\) Regulations 2020](#)) the parties will need to make formal representations to the Administering Authority if they believe an exit credit should be paid outside the policy set out above, or if they dispute the determination of the Administering Authority. The Fund will notify the parties of the information required to make the determination on request.
- If the Fund determines an exit credit is payable then they will pay this directly to the exiting employer within 6 months of completion of the cessation assessment by the Actuary.
- In the case of a deficit, in order to maintain a consistent approach, the Fund will seek to recover this from the exiting employer in the first instance although if this is not possible then the deficit will be recovered from the guarantor either as a further contribution collection or at the next valuation.

In some instances, the outgoing employer may only be responsible for part of the residual deficit or surplus as per the separate risk sharing agreement. The default is that any surplus would be retained by the Fund in favour of the outsourcing employer/guarantor unless representation is made by the relevant parties in line with the Regulations (as noted above). For the avoidance of doubt, where the outgoing employer is not responsible for any costs under a risk sharing agreement then no exit credit will be paid as per the Regulations, provided that the Fund is aware of the provisions of the risk sharing agreement in any representation made.

The Government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment, however the final remedy is not known. Where a surplus or deficit is being subsumed, no allowance will be made for McCloud within the calculations. However, if a representation is made to the Administering Authority then a reasonable estimate for the potential cost of McCloud will need to be included. This will be calculated in line with the treatment set out in this Funding Strategy Statement for all members of the outgoing employer. For the avoidance of doubt, there will be no recourse for an employer with regard to McCloud, once the final termination has been settled and payments have been made. Once the remedy is known, any calculations will be performed in line with the prevailing regulations and guidance in force at the time.

In the event of parties unreasonably seeking to crystallise the exit credit on termination, the Fund will consider its overall policy and seek to recover termination deficits as opposed to allowing them to be subsumed with no impact on contribution requirements until the next assessment of the contribution requirements for the guarantor. Equally where a guarantor decides not to underwrite the residual liabilities then the basis of assessment on termination will assume the liabilities are orphaned and the minimum risk basis of termination will apply.

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

In the case of a surplus, the Fund pays the exit credit to the exiting employer following completion of the termination process (within 6 months of completion of the cessation assessment by the Actuary). This is subject to the exiting employer providing sufficient notice to the Fund of their intent to exit; any delays in notification will impact on the payment date.

In the case of a deficit, the Fund would require the exiting employer to pay the termination deficit to the Fund as an immediate lump sum cash payment (unless agreed otherwise by the Administering Authority at their sole discretion) following completion of the termination process.

The Government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment, however the final remedy is not known. As part of any termination assessment, a reasonable estimate for the potential cost of McCloud will be included. This will be calculated in line with the treatment set out in this Funding Strategy Statement for all members of the outgoing employer. For the avoidance of doubt, there will be no recourse for an employer with regard to McCloud, once the final termination has been settled and payments have been made. Once the remedy is known, any calculations will be performed in line with the prevailing regulations and guidance in force at the time.

The Administering Authority also reserves the right to modify this approach on a case by case basis at its sole discretion if circumstances warrant it based on the advice of the Actuary.

Where an employer with no guarantor leaves the Fund and leaves liabilities with the Fund which the Fund must meet without further recourse to that employer, the valuation of the termination payment will be calculated using the minimum risk basis.

Further details are set out in the termination policy is set out in **Appendix C**.

## **FUNDING FOR EARLY RETIREMENT COSTS**

For those employers not in the Schools/Academies pool, unless allowance is built into the employer's contribution rate, employers are required to meet all costs of early retirement strain by immediate capital payments into the Fund (including those arising from ill-health retirements), or in certain circumstances by agreement with the Fund, through instalments over a period not exceeding 3 years or (if less) the remaining period of the body's membership of the Fund.

For those employers in the Schools/Academies pool, Employers are required to meet the costs of non-ill-health early retirement strains only by immediate capital payments into the Fund, or in certain circumstances by agreement with the Fund, through instalments over a period not exceeding 3 years.

## **FUNDING FOR DEATH BENEFITS**

The financial impact of the benefits that become payable on the death of a member differ depending on whether the member dies before or after retirement.

The extent of any funding strain/profit which emerges on the death of a pensioner member (typically a profit) will be determined by the age of the pensioner at death and whether or not any dependants' benefits become payable.

In the event of a member dying whilst in active service, it is not certain that a funding profit would emerge. Whilst the Fund would no longer have to pay the accrued benefits at retirement for the deceased member, a lump sum death grant and benefits for eligible dependants would become payable instead. The dependants' benefits would also be based on the pensionable service that the member could have accrued had they remained in service until retirement.

Typically, the death of a young member with low pensionable service and eligible dependants is likely to result in a large funding strain for the employer. However, the death of an older/long serving member with no dependants could result in a funding profit. Any funding strain or profit will emerge at the next actuarial valuation through increased/reduced deficit, except where the employer is in the termination process when it will be taken into account when the Actuary determines the termination position.

# 6

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

In assessing the value of the Fund's liabilities in the valuation, allowance has been made for future returns on the Fund's investments, taking into account the investment strategy adopted by the Fund, as set out in the ISS.

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

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

If, at the valuation date, the Fund had been invested in this portfolio, then in carrying out this valuation it would not be appropriate to make any allowance for asset returns above those provided by the minimum risk portfolio, resulting in a negative real return in current market conditions. On this basis of assessment, the assessed value of the Fund's liabilities at the valuation would have been significantly higher, resulting in a funding level of 48%. The difference between this 'minimum risk' measure of the liabilities and the solvency measure gives an indication of the level of reliance on future investment returns within the solvency funding target.

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

The current strategy is:

	Benchmark %
UK Equities	20
Global Equities	40
<b>Total Equities</b>	<b>60</b>
Fixed Income	15
<b>Total Bonds</b>	<b>15</b>
Property	8
Infrastructure	17
<b>Total Alternatives</b>	<b>25</b>
Cash	0
<b>Total</b>	<b>100%</b>

For the purposes of setting a funding strategy, and taking into account the Regulations and guidance, the Administering Authority believes that it is appropriate to take a margin for prudence on the best estimate return expectations emerging from the current strategy (and any potential changes emerging from the investment strategy review being undertaken) (see further comment in Appendix A).

## RISK MANAGEMENT STRATEGY

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

- Equity Protection - the Fund has implemented protection against potential falls in the equity markets via the use of derivatives. The aim of the protection is to provide further stability in employer contributions (all other things equal) in the event of a significant equity market fall (although it is recognised that it will not protect the Fund in totality).

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

# 7

## IDENTIFICATION OF RISKS AND COUNTER-MEASURES

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

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

### FINANCIAL

The financial risks are as follows:-

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

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

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

### DEMOGRAPHIC

The demographic risks are as follows:-

- Future changes in life expectancy (longevity) cannot be predicted with any certainty
- Deteriorating pattern of early retirements (including those granted on the grounds of ill health) over and above what is allowed for in the valuation assumptions;
- Unanticipated acceleration of the maturing of the Fund resulting in materially negative cashflows and shortening of liability durations

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

Ill health retirements can be costly for employers, particularly small employers where one or two costly ill health retirements can take them well above the “average” implied by the valuation assumptions. Increasingly we are seeing employers mitigate the number of ill health retirements by employing HR / occupational health preventative measures. These in conjunction with ensuring the regulatory procedures in place to ensure that ill-health retirements are properly controlled, can help control exposure to this demographic risk.

Apart from the regulatory procedures in place to ensure that ill-health retirements are properly controlled, employing bodies should be doing everything in their power to minimise the number of ill-health retirements, although for some employers, ill-health retirements do not affect the solvency of the Fund because they are the subject of a direct charge.

Similarly, early retirements for reasons of redundancy and efficiency do not affect the solvency of the Fund because they too are the subject of a direct charge.

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

## **INSURANCE OF CERTAIN BENEFITS**

The contributions for any employer may be varied as agreed by the Actuary and Administering Authority to reflect any changes in contribution requirements as a result of any benefit costs being insured with a third party or internally within the Fund.

## **REGULATORY**

The key regulatory risks are as follows:-

- Changes to Regulations, e.g. changes to the benefits package, retirement age, potential new entrants to Fund;
- Changes to national pension requirements and/or HMRC Rules.

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

## **GOVERNANCE**

The Fund has done as much as it believes it reasonably can to enable employing bodies and Fund members (via their representatives on the Local Pension Board) to make their views known to the Fund and to participate in the decision-making process.

Governance risks are as follows:-

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

- An employer ceasing to exist with insufficient funding or adequacy of a bond;
- An employer ceasing to exist without prior notification, resulting in a large exit credit requirement from the Fund impacting on cashflow requirements;
- Changes in the Committee membership.

For these risks to be minimised much depends on information being supplied to the Administering Authority by the employing bodies. Arrangements are strictly controlled and monitored, but in most cases the employer, rather than the Fund as a whole, bears the risk.

### **LOCAL PENSION BOARD**

The Pension Board was established in April 2015 in accordance with the Public Service Pensions Act 2013, the national statutory governance framework delivered through the LGPS Regulations and guidance as issued by the Scheme Advisory Board.

The Board seeks to assist the London Borough of Waltham Forest to maintain effective and efficient administration and governance. The LPB comprises Fund members, both retired and active, together with employer representatives.

It meets quarterly and all Board Members have undertaken training and have established a work programme that will enable them to meet their obligations to ensure that the Fund complies with the relevant codes of practice and current legislation.

# 8

## MONITORING AND REVIEW

The Administering Authority has taken advice from the actuary in preparing this Statement, and has consulted with the employers participating in the Fund.

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

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

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

When monitoring the funding strategy, if the Administering Authority considers that any action is required, the relevant employing authorities will be contacted. In the case of admitted bodies, there is statutory provision for rates to be amended between valuations and this will be considered in conjunction with the employer affected and any associated guarantor of the employer's liabilities (if relevant).

### **COST MANAGEMENT AND THE MCCLOUD JUDGMENT**

The cost management process was set up by HMT, with an additional strand set up by the Scheme Advisory Board (for the LGPS). The aim of this was to control costs for employers and taxpayers via adjustments to benefits and/or employee contributions.

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

The outcomes of the cost management process were expected to be implemented from 1 April 2019, based on data from the 2016 valuations for the LGPS. This has now been put on hold due to age discrimination cases brought in respect of the firefighters and judges schemes ('the McCloud judgment'), relating to protections provided when the public sector schemes were changed (which was on 1 April 2014 for the LGPS and 1 April 2015 for other schemes).

It is not known how these cases will affect the LGPS or the cost management process at this time. The Scheme Advisory Board has issued guidance on how the McCloud judgment should be allowed for within the 2019 valuation.

The potential impact of the McCloud judgment (based on the information currently available) has been quantified and communicated to employers as part of the 2019 valuation. This has been assessed by removing the current age criteria applied to the underpin implemented in 2014 for the LGPS. This underpin therefore would apply to all active members as at 1 April 2012. Employers will be able to choose to include these estimated costs over 2020/23 in their certified contributions. Alternatively, if they choose not to do this, they will need to make allowance within their budgets for the potential costs and note that backdated contributions could become payable if the remedy becomes known before the next valuation.

# APPENDIX A – ACTUARIAL METHOD AND ASSUMPTIONS

## METHOD

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

## FINANCIAL ASSUMPTIONS – SOLVENCY FUNDING TARGET AND COST OF FUTURE ACCRUAL

### Investment return (discount rate) – Solvency Funding Target

The discount rate has been derived based on the expected return on the Fund assets based on the long term strategy set out in the Investment Strategy Statement (ISS). It includes appropriate margins for prudence. When assessing the appropriate discount rate consideration has been given to the returns in excess of CPI inflation (as derived below). The discount rate at the valuation has been derived based on an assumed return of 1.95% per annum above CPI inflation, i.e. a total discount rate of 4.35% per annum. This real return will be reviewed from time to time based on the investment strategy, market outlook and the Fund's overall risk metrics.

### Investment return (discount rate) – Cost of Future Accrual

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

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

The financial assumptions in relation to future service (i.e. the normal cost) are based on an overall assumed real discount rate of 2.5% per annum above the long term average assumption for consumer price inflation of 2.4% per annum. This leads to a discount rate of 4.9% per annum.

### Inflation (Consumer Prices Index)

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

The overall reduction to RPI inflation at the valuation date is 1.0% per annum. The CPI inflation assumption at the valuation date is 2.4% per annum. =This adjustment to the RPI inflation assumption will be reviewed from time to time to take into account any reform of the RPI index as announced by the Chancellor in the March 2020 budget. Any change will then be implemented for all relevant policies in this Funding Strategy Statement.

### **Salary increases**

In relation to benefits earned prior to 1 April 2014, and to allow for any final salary 'underpin' applying to benefits earned after that date, the assumption for real salary increases (salary increases in excess of price inflation) will be 1.5% p.a. over the CPI inflation assumption as described above. This includes allowance for promotional increases and represents the long term salary increase assumption. In the shorter term, for certain employers, allowance may be made for a lower rate of salary increase to apply. In such circumstances, the default assumption is for pay growth of 2% (covering both headline increases and incremental drift) each year from the valuation date up to 31st March 2023. Employers will be able to opt for the long-term assumption only should they wish.

Application of bespoke salary increase assumptions as put forward by individual employers will be at the ultimate discretion of the Administering Authority but must be reasonable and practical. Employers will need to provide clear evidence that justifies any bespoke assumptions (for example a long-term pay agreement). To the extent that experience differs to the assumption adopted, the effects will emerge at the next actuarial valuation.

### **Pension increases/Indexation of CARE benefits**

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

## **DEMOGRAPHIC ASSUMPTIONS**

### **Mortality/Life Expectancy**

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

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

### Commutation

It has been assumed that, on average, retiring members will take 80% of the maximum tax-free cash available at retirement. This is broadly equivalent to the assumption at the 2016 actuarial valuation. The option which members have to commute part of their pension at retirement in return for an additional lump sum is based on a rate of £12 cash for each £1 p.a. of pension given up.

### Other Demographics

Following an analysis of Fund experience carried out by the Actuary, the proportions married/civil partnership assumption, rates of ill-health retirement (for some employers) and withdrawal from active service assumption have been retained from the last valuation. No allowance will be made for the future take-up of the 50:50 option. Where any member has actually opted for the 50:50 scheme, this will be allowed for in the assessment of the rate for the next 3 years. Other assumptions are as per the last valuation.

### Expenses

Expenses are met out the Fund, in accordance with the Regulations. This is allowed for by adding 0.7% of pensionable pay to the contributions required from participating employers. This addition is reassessed at each valuation. Investment expenses have been allowed for implicitly in determining the discount rates.

### Discretionary Benefits

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

## METHOD AND ASSUMPTIONS USED IN CALCULATING RECOVERY PLAN CONTRIBUTIONS (OR SECONDARY RATE)

### Allowance for asset backed guarantees

For one employer, London Borough of Waltham Forest, when determining contributions payable to recover its shortfall, allowance has been made for the value of residual property investments currently held in a Special Purpose Vehicle that will be gifted to the Fund in 38 years' time. The value of the gift makes the following assumptions:

- Useful lifetime of properties for residential rental purposes – 38 years from 2020 = 38 years
- Discount rate to value rental income – gilts plus 3.4% per annum, to reflect broadly the yield required from an investor in this type of arrangement. Subject to being no less than the valuation discount rate.
- Recovery period for spreading value of rental income against deficit reduction contributions – 19 years.
- Indexation of rental income – 2% per annum.
- Rental income lost through voids and bad debts from time 38 years onwards – 5.75% of total rental income per annum.
- Property management and refurbishment costs – 30% of total rental income per annum.

## EMPLOYER ASSET SHARES

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

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

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

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

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

<b>Long-term yields</b>	
Market implied RPI inflation	3.40% p.a.
<b>Solvency Funding Target financial assumptions</b>	
Investment return/Discount Rate	4.35% p.a.
CPI price inflation	2.40% p.a.
Long Term Salary increases*	3.90% p.a.
Pension increases/indexation of CARE benefits**	2.40% p.a.
<b>Future service accrual financial assumptions</b>	
Investment return/Discount Rate	4.90% p.a.
CPI price inflation	2.40% p.a.
Long Term Salary increases*	3.90% p.a.
Pension increases/indexation of CARE benefits	2.40% p.a.

\* in addition to this, an allowance for further short-term pay restraint may be made. This will be 2% per annum for 4 years to 31 March 2023 depending on an employer’s circumstances.

\*\* for those members reaching State Pension Age between 6 April 2016 and 5 April 2021, full CPI increases on Guaranteed Minimum Pensions have been assumed once in payment. Otherwise statutory increases on Guaranteed Minimum Pension will apply e.g. nil on Guaranteed Minimum Pensions accrued prior to 6 April 1988 and in line with CPI (subject to a maximum of 3% p.a.) for Guaranteed Minimum Pensions accrued after 5 April 1988.

**Life expectancy assumptions**

The post retirement mortality tables adopted for this valuation, along with sample life expectancies, are set out below:

*-Post retirement mortality tables*

<b>Current Status</b>	<b>Retirement Type</b>	<b>Mortality Table</b>
<b>Annuitant</b>	Normal Health	99% S3PMA_CMI_2018 [1.75%] 90% S3PFA_M_CMI_2018 [1.75%]
	Dependant	134% S3PMA_CMI_2018 [1.75%] 91% S3DFA_CMI_2018 [1.75%]
	Ill Health	116% S3IMA_CMI_2018 [1.75%] 138% S3IFA_CMI_2018 [1.75%]
	Future Dependant	125% S3PMA_CMI_2018 [1.75%] 107% S3DFA_CMI_2018 [1.75%]
<b>Active</b>	Normal Health	104% S3PMA_CMI_2018 [1.75%] 92% S3PFA_M_CMI_2018 [1.75%]

	Ill Health	121% S3IMA_CMI_2018 [1.75%] 141% S3IFA_CMI_2018 [1.75%]
<b>Deferred</b>	All	125% S3PMA_CMI_2018 [1.75%] 104% S3PFA_M_CMI_2018 [1.75%]
<b>Future Dependant</b>	Dependant	132% S3PMA_CMI_2018 [1.75%] 114% S3DFA_CMI_2018 [1.75%]

*-Life expectancies at age 65*

Membership Category	Male Life Expectancy at 65	Female Life Expectancy at 65
Pensioners	22.5	25.0
Actives aged 45 now	24.1	26.9
Deferreds aged 45 now	22.7	26.0

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

# APPENDIX B – EMPLOYER DEFICIT / SURPLUS RECOVERY PLANS

For certain employers, as the assets of the Fund are less than the liabilities at the effective date, a deficit recovery plan needs to be adopted such that additional contributions are paid into the Fund to meet the shortfall.

Deficit contributions paid to the Fund by each employer will be expressed as £s amounts (unless otherwise agreed with the Administering Authority) increasing at 3.9% per annum (in line with the long-term pay growth assumption) and it is the Fund's objective that any funding deficit is eliminated as quickly as the participating employers can reasonably afford based on the Administering Authority's view of the employer's covenant and risk to the Fund.

Recovery periods will be set by the Fund on a consistent basis across employer categories where possible and communicated as part of the discussions with employers. This will determine the minimum contribution requirement, with employers free to select any shorter deficit recovery period and higher contributions if they wish, including the option of prepaying the deficit contributions in one lump sum either on an annual basis or via a one-off payment. Any early payment will be allowed for in the monetary amount requested via a reduction in the overall £ deficit contributions otherwise payable.

The determination of the recovery periods is summarised in the table below:

Category	Default Deficit Recovery Period	Derivation
Fund Employers	19 years	Determined by maintaining the period from the preceding valuation and to ensure, where appropriate, contributions do not reduce versus those expected from the existing recovery plan.
Open Admitted Bodies	19 years	Determined by maintaining the period from the preceding valuation and to ensure, where appropriate, contributions do not reduce versus those expected from the existing recovery plan.
Closed Employers	Lower of 19 years and the future working lifetime of the membership	Determined by maintaining the period from the preceding valuation and to ensure, where appropriate, contributions do not reduce versus those expected from the existing recovery plan.
Employers with a limited participation in the Fund	Determined on a case by case basis	Length of expected period of participation in the Fund. Generally for those employers providing a service this will be contract length.

In determining the actual recovery period to apply for any particular employer or employer grouping, the Administering Authority may take into account some or all of the following factors:

- The size of the funding shortfall;
- The business plans of the employer;
- The assessment of the financial covenant of the employer, and security of future income streams;
- Any contingent security available to the Fund or offered by the employer such as guarantor or bond arrangements, charge over assets, etc.

The objective is to recover any deficit over a reasonable timeframe, and this will be periodically reviewed. Subject to affordability considerations a key principle will be to maintain the deficit contributions at the expected monetary levels from the preceding valuation (allowing for any indexation in these monetary payments over the recovery period) taking into account any changes in the primary rate contribution requirements.

For those employers assessed to be in surplus at the valuation date, the surplus will be removed over a maximum recovery period of 19 years, unless agreed otherwise with the administering authority.

### **Other factors affecting the Employer Deficit Recovery Plans**

As part of the process of agreeing funding plans with individual employers and managing risk in the inter-valuation period, the Administering Authority will consider the use of contingent assets and other tools such as bonds or guarantees that could assist employing bodies in managing the cost of their liabilities or could provide the Fund with greater security against outstanding liabilities. All other things equal this could result in a longer recovery period being acceptable to the Administering Authority, although employers will still be expected to at least cover expected interest costs on the deficit.

It is acknowledged by the Administering Authority that, whilst posing a relatively low risk to the Fund as a whole, a number of smaller employers may be faced with significant contribution increases that could seriously affect their ability to function in the future. The Administering Authority therefore may in some cases be willing to use its discretion to accept an evidence based affordable level of contributions for such organisations for the three years 2020/23. Any application of this option is at the ultimate discretion of the Fund officers and Section 151 officer in order to effectively manage risk across the Fund. It will only be considered after the provision of the appropriate evidence as part of the covenant assessment and the receipt of appropriate professional advice.

For those bodies identified as having a weaker covenant, the Administering Authority will need to balance the level of risk plus the solvency requirements of the Fund with the sustainability of the organisation when agreeing funding plans. As a minimum, the annual deficit payment must meet the ongoing interest costs to ensure, everything else being equal, that the deficit does not increase in monetary terms.

Notwithstanding the above, the Administering Authority, in consultation with the actuary, will also consider whether any exceptional arrangements should apply in particular cases.

# APPENDIX C –

## ADMISSION AND TERMINATION POLICY

This document details the London Borough of Waltham Forest Pension Fund's (LBWPF) policy on the methodology for assessment of ongoing contribution requirements and termination payments in the event of the cessation of an employer's participation in the Fund. This document also covers LBWPF's policy on admissions into the Fund and sets out the considerations for current and former admission bodies. It supplements the general policy of the Fund.

A list of all current employing bodies participating in the LBWPF is kept as a live document and will be updated by the Administering Authority as bodies are admitted to, or leave the LBWPF.

Please see the glossary for an explanation of the terms used throughout this Appendix.

### ENTRY TO THE FUND

#### MANDATORY SCHEME EMPLOYERS

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

#### DESIGNATING BODIES

Designating bodies are permitted to join the scheme if they pass a resolution to this effect. Designating bodies, other than connected entities, are not required under the Regulations to provide a guarantee. These bodies usually have tax raising powers and include Parish and Town Councils.

#### ADMISSION BODIES

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

Admitted bodies can join the Fund if:

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

In general, admitted bodies may only join the Fund if they are guaranteed by a scheme employer. However, there may be exceptional circumstances whereby, subject to the agreement of the Administering Authority, an admitted body joins the Fund with an alternative form of guarantee. When the agreement or service provision ceases, the Fund's policy is that in all cases it will look to recover any outstanding deficit from the outgoing body unless appropriate instruction is received from the outsourcing employer or guaranteeing employer, in which case the assets and liabilities of the admission body will in revert to the outsourcing scheme employer or guaranteeing employer.

## CONNECTED ENTITIES

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

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

To limit the risk to the Fund, the Fund will require that the scheme employer provides a guarantee for their connected entity, in order that the ongoing funding basis will be applied to value the liabilities.

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

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

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

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

## RISK ASSESSMENTS

Prior to admission to the Fund, an Admitted Body is required to carry out an assessment of the level of risk on premature termination of the contract to the satisfaction of the Administering Authority. If the risk assessment and/or bond amount is not to the satisfaction of the Administering Authority (as required under the LGPS Regulations) it will consider and determine whether the admission body must pre-fund for termination with contribution requirements assessed using the minimum risk methodology and assumptions.

Some aspects that the Administering Authority may consider when deciding whether to apply a minimum risk methodology are:

- Uncertainty over the security of the organisation's funding sources e.g. the body relies on voluntary or charitable sources of income or has no external funding guarantee/reserves;
- If the admitted body has an expected limited lifespan of participation in the Fund;
- The average age of employees to be admitted and whether the admission is closed to new joiners.

In order to protect other Fund employers, where it has been considered undesirable to provide a bond, a guarantee must be sought in line with the LGPS Regulations.

## ADMITTED BODIES PROVIDING A SERVICE

Generally Admitted Bodies providing a service will have a guarantor within the Fund that will stand behind the liabilities. Accordingly, in general, the minimum risk approach to funding and termination will not apply for these bodies.

As above, the Admitted Body is required to carry out an assessment of the level of risk on premature termination of the contract to the satisfaction of the Administering Authority. This assessment would normally be based on advice in the form of a "risk assessment report" provided by the actuary to the LBWFPPF. As the Scheme Employer is effectively the ultimate guarantor for these admissions to the LBWFPPF it must also be satisfied (along with the Administering Authority) over the level (if any) of any bond requirement. Where bond agreements are to the satisfaction of the Administering Authority, the level of the bond amount will be subject to review on a regular basis.

In the absence of any other specific agreement between the parties, deficit recovery periods for Admitted Bodies will be set in line with the Fund's general policy as set out in the FSS.

Any risk sharing arrangements agreed between the Scheme Employer and the Admitted Body will be documented in the commercial agreement between the two parties and not the admission agreement.

In the event of termination of the Admitted Body, any orphan liabilities in the Fund will be subsumed by the relevant Scheme Employer.

An exception to the above policy applies if the guarantor is not a participating employer within the LBWFPPF, including if the guarantor is a participating employer within another LGPS Fund. In order to protect other employers within the LBWFPPF the Administering Authority may in this case treat the admission body as pre-funding for termination, with contribution requirements assessed using the minimum risk methodology and assumptions

## CONTRIBUTION RATE ASSESSMENTS

For any Admitted Body for whom the Scheme Employer is in the Schools/Academies pool, the contribution rate payable will be in line with the total contribution rate payable by the pool, as assessed as part of each triennial actuarial valuation (see Appendix D). The Admitted Body then also becomes part of the pool.

Where the Scheme Employer is a stand-alone Academy, and there are less than or equal to 10 members transferring at the point of admission, the Admitted Body will pay the same Primary Contribution Rate as the Scheme Employer.

Where there are more than 10 members transferring at the point of admission, or the Scheme Employer is not an Academy (e.g. the Council), the Actuary will undertake an assessment of the required contribution rate payable.

## PRE-FUNDING FOR TERMINATION

An employing body may choose to pre-fund for termination i.e. to amend their funding approach to a minimum risk methodology and assumptions. This will substantially reduce the risk of an uncertain and potentially large debt being due to the Fund at termination. However, it is also likely to give rise to a substantial increase in contribution requirements.

For any employing bodies funding on such a minimum risk strategy a notional liability matching investment strategy will be assumed. In particular, the employing body's notional asset share of the Fund will be credited with an investment return in line with the minimum risk funding assumptions adopted rather than the actual investment return generated by the actual asset portfolio of the entire Fund. The Fund reserves the right to modify this approach in any case where it might materially affect the finances of the Scheme, or depending on any case specific circumstances.

## EXITING THE FUND

### TERMINATION OF AN EMPLOYER'S PARTICIPATION

When an employer's participation in the Fund comes to its end, or is prematurely terminated for any reason (e.g. a contract with a local authority comes to an end or the employer chooses to voluntarily cease participation), employees may transfer to another employer, either within the Fund or elsewhere. If this is not the case the employees will retain pension rights within the Fund either as deferred benefits or immediate retirement benefits.

In addition to any liabilities for current employees the Fund will also retain liability for payment of benefits to former employees, i.e. to existing deferred and pensioner members except where there is a complete transfer of responsibility to another Fund with a different Administering Authority.

Where the Fund obtains advance notice that an employer's participation is coming to an end, the Regulations enable the Fund to commission a funding assessment leading to a revised contribution certificate which is designed to eliminate, as far as possible, any surplus or deficit by the cessation date.

Whether or not an interim contribution adjustment has been initiated once participation in the Fund has ceased, the employer becomes an exiting employer under the Regulations and the Fund is then required to obtain an actuarial valuation of that employer's liabilities in respect of benefits of the exiting employer's current and former employees along with a revision of the rates and adjustment certificate showing any contributions due from the admission body.

When an employer exits the Fund, as an alternative to requiring an immediate payment in full, the Regulations give power to the Fund to set a repayment plan to recover the outstanding debt over a period at the sole discretion of the Administering Authority. Whether this will be permitted will depend on the affordability of the repayments and financial strength of the exiting employer. Once any such repayment plan is set the payments would not be reviewed for changes in the funding position due to market or demographic factors.

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

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

In the event that unfunded liabilities arise that cannot be recovered from the employing body, these will normally fall to be met by the Fund as a whole (i.e. all employers) unless there is a guarantor or successor body within the Fund.

## **BASIS OF TERMINATION**

For those employing bodies who joined the Fund after 30 September 2009, the LBWFPP's policy is that a termination assessment will be made based on a minimum risk funding basis, unless the employing body has a guarantor within the Fund or a successor body exists to take over the employing body's liabilities (including those for former employees). This is to protect the other employers in the Fund as, at termination, the employing body's liabilities will become orphan liabilities within the Fund, and there will be no further recourse to the exiting employer if a shortfall emerges in the future (after participation has terminated).

Details of the minimum risk funding basis are shown below.

If, instead, the employing body has a guarantor within the Fund or a successor body exists to take over the employing body's liabilities, the LBWFPP's policy is that the valuation funding basis will be used for the termination assessment unless the guarantor informs the LBWFPP otherwise. The guarantor or successor body will then, following any termination payment made, subsume the assets and liabilities of the employing body within the Fund. (For Admission Bodies, this process is sometimes known as the "novation" of the admission agreement.) This may, if agreed by the successor body, constitute a complete amalgamation of assets and liabilities to the successor body, including any funding deficit on closure. In these circumstances no termination payment will be required from the outgoing employing body itself, as the deficit would be recovered via the successor body's own deficit recovery plan.

For those employing bodies who joined the Fund prior to 30 September 2009, the LBWFPPF policy is that these existing admissions will be notionally “ring-fenced” with the valuation funding basis used for the termination assessment and calculation of ongoing contribution requirements. In the event that unfunded liabilities arise that cannot be recovered from the admission body at termination and in the absence of a guarantor or successor body, these will fall to be met by the Fund as a whole.

It is possible under certain circumstances that an employer can apply to transfer all assets and current and former members’ benefits to another LGPS Fund in England and Wales. In these cases, no termination assessment is required as there will no longer be any orphan liabilities in the LBWFPPF. Therefore, a separate assessment of the assets to be transferred will be required.

## IMPLEMENTATION

### ADMISSION BODIES PARTICIPATING BY VIRTUE OF A CONTRACTUAL ARRANGEMENT

For employers that are guaranteed by a guarantor (usually the original employer or letting authority), the Fund’s policy at the point of cessation is for the guarantor to subsume the residual assets, liabilities and any surplus or deficit under the default policy. In some instances an exit debt may be payable by an employer before the assets and liabilities are subsumed by the guarantor, this will be considered on a case-by-case basis. No payment of an exit credit will be payable unless representation is made as set out below.

If there is any dispute, then the following arrangements will apply:

- In the case of a surplus, in line with the amending Regulations ([The Local Government Pension Scheme \(Amendment\) Regulations 2020](#)) the parties will need to make representations to the Administering Authority if they believe an exit credit should be paid outside the policy set out above, or if they dispute the determination of the Administering Authority. The Fund will notify the parties of the information required to make the determination on request.
- If the Fund determines an exit credit is payable then they will pay this directly to the exiting employer within 6 months of completion of the cessation assessment by the Actuary.
- In the case of a deficit, in order to maintain a consistent approach, the Fund will seek to recover this from the exiting employer in the first instance although if this is not possible then the deficit will be recovered from the guarantor either as a further contribution collection or at the next valuation.

In some instances, the outgoing employer may only be responsible for part of the residual deficit or surplus as per the separate risk sharing agreement. The default is that any surplus would be retained by the Fund in favour of the outsourcing employer/guarantor unless representation is made by the relevant parties in line with the Regulations as noted above. For the avoidance of doubt, where the outgoing employer is not responsible for any costs under a risk sharing agreement then no exit credit will be paid as per the Regulations unless the Fund is aware of the provisions of the risk sharing agreement in any representation made and determines an exit credit should be paid.

The Government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment, however the final remedy is not known. Where a surplus or deficit is being subsumed, no allowance will be made for McCloud within the calculations. However, if a representation is made to the Administering Authority then a reasonable estimate for the potential cost of McCloud will need to be included. This will be calculated in line with the treatment set out in this Funding Strategy Statement for all members of the outgoing employer. For the avoidance of doubt, there will be no recourse for an employer with regard to McCloud, once the final termination has been settled and payments have been made. Once the remedy is known, any calculations will be performed in line with the prevailing regulations and guidance in force at the time.

In the event of parties unreasonably seeking to crystallise an exit credit on termination the Fund will consider its overall policy and seek to recover termination deficits as opposed to allowing them to be subsumed with no impact on contribution requirements until the next assessment of the contribution requirements for the guarantor. Equally where a guarantor decides not to underwrite the residual liabilities then the termination assessment will assume the liabilities are orphaned and the minimum risk basis of termination will be applied.

As the guarantor will absorb the residual assets and liabilities under the default policy above, it is the view of the Actuary that the ongoing valuation basis described above should be adopted for the termination calculations. This is the way the initial admission agreement would typically be structured i.e. the admission would be fully funded based on liabilities assessed on the valuation basis.

If the guarantor refuses to take responsibility, then the residual deferred pensioner and pensioner liabilities should be assessed on the more cautious minimum risk basis. In this situation the size of the termination payment would also depend on what happened to the active members and if they all transferred back to the original Scheme Employer (or elsewhere) and aggregated their previous benefits. As the transfer would normally be effected on a "fully funded" valuation basis the termination payment required would vary depending on the circumstances of the case. Where this occurs the exiting employer would then be treated as if it had no guarantor as per the policy below.

The Administering Authority also reserves the right to modify this approach on a case by case basis at its sole discretion if circumstances warrant it based on the advice of the Actuary, based on representations from the interested parties where appropriate.

## **NON CONTRACT BASED ADMISSION BODIES WITH A GUARANTOR IN THE FUND**

The approach for these will be the same as for contract based admission bodies above and will depend on whether the guarantor is prepared to accept responsibility for residual liabilities. Indeed, it may be that Fund is prepared to accept that no actual termination payment is needed (even if one is calculated) and that all assets/liabilities can simply be absorbed by the guarantor.

## ADMISSION BODIES WITH NO GUARANTOR IN THE FUND

These are the cases where the residual liabilities would be orphaned within Fund. It is possible that a bond would be in place. The termination calculation would be on the more cautious “minimum risk” basis.

The actuarial valuation and the revision of any Rates and Adjustments Certificate in respect of the outgoing admission body must be produced by the Actuary at the time when the admission agreement ends; the policy will always be subject to change in the light of changing economic circumstances and legislation.

The policy for such employers will be:

- In the case of a surplus, the Fund pays the exit credit to the exiting employer following completion of the termination process (within 6 months of completion of the cessation by the Actuary). This is subject to the exiting employer providing sufficient notice to the Fund of their intent to exit; any delays in notification will impact on the payment date.
- In the case of a deficit, the Fund would require the exiting employer to pay the termination deficit to the Fund as an immediate lump sum cash payment (unless agreed otherwise by the Administering Authority at their sole discretion) following completion of the termination process.

The Government has confirmed that a remedy is required for the LGPS in relation to the McCloud judgment, however the final remedy is not known. As part of any termination assessment, a reasonable estimate for the potential cost of McCloud will be included. This will be calculated in line with the treatment set out in this Funding Strategy Statement for all members of the outgoing employer. For the avoidance of doubt, there will be no recourse for an employer with regard to McCloud, once the final termination has been settled and payments have been made. Once the remedy is known, any calculations will be performed in line with the prevailing regulations and guidance in force at the time.

The Administering Authority also reserves the right to modify this approach on a case by case basis at its sole discretion if circumstances warrant it based on the advice of the Actuary.

The above funding principles will also impact on the **bond requirements** for certain admitted bodies. The purpose of the bond is that it should cover any unfunded liabilities arising on termination that cannot be reclaimed from the outgoing body.

## CONNECTED ENTITIES

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

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

## RELEVANT REGULATIONS WITHIN THE LOCAL GOVERNMENT PENSION SCHEME REGULATIONS 2013 (AS AMENDED BY THE LOCAL GOVERNMENT PENSION SCHEME (AMENDMENT) REGULATIONS 2018)

Regulation 64 sets out special circumstances where revised actuarial valuations and certificates must be obtained including Regulation 64 (2) where an admission agreement ceases to have effect, the Administering Authority who made it must obtain:

- an actuarial valuation as at the date it ceases the liabilities in respect of current and former employees of the admission body which is a party to that admission agreement ("the outgoing admission body");
- a revision of any rates and adjustments certificate for any Pension Fund which is affected, showing the exit payment due from the exiting body or exit credit payable to the exiting body. Where it is not possible for any reason to obtain revised contributions from the exiting body, or from an insurer or any person providing an indemnity or bond on behalf of the body, the Administering Authority may obtain a further revision of any rates and adjustment certificate for the Pension Fund, showing:
  - a) in the case where the exiting body falls within paragraph 1(d) of Part 3 of Schedule 2 the revised contributions due from the body which is the related employer in relation to that admission body; and
  - b) in any other case, the revised contributions due from each employing authority who contributes to the Fund.

If the Administering Authority becomes aware or is of the opinion of a scheme employer becoming an exiting employer, Regulation 64 (4) provides that it may obtain from an actuary a certificate specifying, in the case of an admission body, the percentage or amount by which, in the actuary's opinion:

- the contribution at the primary rate should be adjusted; or
- any prior secondary rate adjusted should be increased or reduced, with a view to providing that assets equivalent to the exit payment that will fall due from the Scheme employer are provided to the Fund by the likely exit date or, where the scheme employer is unable to meet the liability by that date, over such period of time thereafter as the Administering Authority considers reasonable.

## MINIMUM RISK TERMINATION BASIS

The minimum risk financial assumptions that applied at the actuarial valuation date (31 March 2019) are set out below in relation to any liability remaining in the Fund. These will be updated on a case-by-case basis, with reference to prevailing market conditions at the relevant employing body's cessation date.

<b>Least risk assumptions</b>	<b>31 March 2019</b>
Discount Rate	1.5% p.a.
CPI price inflation	2.4% p.a.
Pension increases/indexation of CARE benefits	2.4% p.a.

All demographic assumptions will be the same as those adopted for the 2019 actuarial valuation, except in relation to the life expectancy assumption. Given the minimum risk financial assumptions do not protect against future adverse demographic experience a higher level of prudence will be adopted in the life expectancy assumption.

The termination basis for an outgoing employer will include an adjustment to the assumption for longevity improvements over time by increasing the long term rate of improvement in mortality rates to 2% p.a. from 1.75% p.a. as used in the 2019 valuation for ongoing funding and contribution purposes. This assumption will be reviewed from time to time to allow for any material changes in life expectancy trends and will be formally reassessed at the next valuation.

In addition, since the valuation date, it has been announced that RPI inflation is likely to be reformed with the reform potentially meaning the index is closer to the CPIH inflation measure. This would need to be reflected when deriving an updated market estimate of CPI inflation. For example when assessing a termination position (at February 2020) we will adjust the market RPI inflation to arrive at the CPI inflation assumption by deducting 0.7% per annum as opposed to the 1.0% per annum at the valuation date when assessing an employer's termination position. This adjustment will be kept under review as more details emerge on the reform of RPI.

# APPENDIX D –

## ACADEMIES POLICY

### 1. INTRODUCTION

1.1 The Local Government Pension Scheme (LGPS) Miscellaneous Regulations 2010 made an amendment to the LGPS (Administration) Regulations 2008 to allow an Academy established under the Academies Act 2010, to become a Scheme Employer within the LGPS.

1.2 The Department for Education issued guidance that indicated a newly converted Academy would be expected to assume responsibility for an initial funding deficit and that Academies would operate under a minimum notice period of 7 years.

1.3 A note was subsequently issued by the Secretaries of State for Education and Communities and Local Government in December 2011 that stated Academies' overall pension costs should not increase as a result of conversion and that pooling arrangements should be considered positively.

1.4 This document details the London Borough of Waltham Forest Pension Fund's ("the Fund") policy on the pension funding options available to newly formed Academies.

### 2. APPROACH

2.1 Prior to 1 July 2012, before converting to Academy status, schools had been pooled together with the Local Education Authority (LEA) including other LEA schools and other Council departments for the purpose of meeting their obligations for LGPS pension provision, in particular for the assessment of employer contribution rates.

2.2 All of the LEA's and LEA schools' active members on 1 July 2012 were re-classified as a new distinct group separate from the other Council departments. This group were constituted as the Schools/Academies Group ("the Group").

2.3 An amount of pension fund assets (minimum of nil) was notionally transferred to the Group from the Council's section of the Fund such that the deficit recovery contributions required from the Group to repair the resultant deficit were maintained at the same level (at the time of re-classification) as those required prior to re-classification.

2.4 The required employer contributions will be driven by the profile and underlying funding position of the Group as a whole. It will be periodically assessed at each triennial actuarial valuation of the Fund, in accordance with the Fund's Funding Strategy Statement, as if the Group was an individual employer.

2.6 For individual employers within the Group, the treatment described in 2.4 means that the contributions payable could be more, or less, than would be required if that employer was classed as a separate entity within the Fund.

2.7 The Administering Authority retains the ultimate discretion in applying this policy and will consider any representations made to it on a case-by-case basis. Any variations agreed however will take into account the covenant / financial strength of the body concerned.

### 3 OPTIONS

3.1 The Fund offered existing Academies Act 2010 Academies (i.e. those that converted to Academy status before 1 July 2012) a one-off choice, see paragraph 4.12, in respect of their treatment within the Fund going forward:

3.1.1 Such academies either elected to participate within the Group effective from 1 April 2014 and adopt the pooled Group contribution rate, or

3.1.2 They elected to continue being treated as a separate entity. That is, they remained as a stand-alone employer within the Fund entirely responsible for their own membership experiences and only theirs rather than a wider group.

3.2 The contribution rates payable by all employers in the Fund include a contribution towards the cost of pension benefits to be accrued in the future and a contribution towards the cost of repairing any funding deficit in respect of benefits accrued to date. As outlined in paragraph 2.4, under a pooled arrangement, the membership profile and level of past service deficit will drive the contribution requirement and will be assessed across all pooled employers. Under a stand-alone arrangement, the circumstances of the single employer will determine the contribution requirements.

3.3 Once a decision has been reached in terms of the choice available to an Academy as outlined in 3.1, this cannot be reversed by the Academy. There may be circumstances however where there may be a Regulatory requirement for a reversal to take place. The Council, as Administering Authority, also reserves the right to reconsider the funding treatment of the Academies (alongside other admitted bodies).

### POOLING

3.4 By pooling within the Group, there will be a cross subsidy of cost between participating employers within the Group. Under a pooled arrangement a participating employer would be exposed to the experience of the Group as a whole, in terms of the risks associated with pension funding and vice-versa e.g. pay growth, ill-health retirement, mortality experience etc. The approach, therefore, could have the effect that the contributions payable to the Fund are more, or less, than would be required if a participating employer was classed as a separate entity.

3.5 Implementation and Operation rules will be as set out below in section 4, relating to:

- a new conversion to Academy status for a School already participating within the Group,
- a new conversion to Academy status for a School already participating within the Group where the new Academy will participate in a different LGPS Fund, and
- an Academy ceasing to operate and policy around the assessment / recovery of any underfunding.

3.6 The Group will be subject to the funding parameters as set out in the Fund's Funding Strategy Statement, which governs how contribution rates are determined at each formal actuarial valuation (see 2.4).

## 4 IMPLEMENTATION AND OPERATION

### NEW ACADEMIES

4.1 Any Schools within the Group that, in future, elect to convert to Academy status will remain part of the Group but re-classified to an Academy and will continue to pay the pooled Group contribution rate effective at their conversion date. The pooled Group contribution rate will be reassessed at each triennial actuarial valuation.

### CHANGES OF FUND

4.3 For any School electing to convert to an Academy that would participate in another LGPS Fund, the bulk transfer arrangements required would be constructed such that an amount of pension fund assets (minimum of nil), determined as at conversion date, will be transferred from the Group to the receiving LGPS Fund such that, assuming no change to the deficit recovery period, the deficit recovery contributions required, in respect of the transferring members, will be maintained at the same level post transfer as those required prior to transfer (in either £s or % of pay terms, as appropriate). This is consistent with the approach adopted, where there is no change in Fund, as set out in this policy document. The amount of assets ultimately transferred to another LGPS Fund will be the amount determined at conversion date, updated to allow for Fund investment returns since conversion date, where available, or appropriate index returns where Fund returns over the period are unavailable.

### ACADEMY CLOSURES

4.4 Where an Academy within the Group ceases, a termination assessment will be performed in accordance with the Regulations. Where the Group as a whole remains in deficit (as assessed at the most recent actuarial valuation), a termination contribution payable by the outgoing body to the Group will be calculated by the Fund Actuary. The termination payment will be calculated as the capitalised amount, as at the date of closure, of all future deficit recovery contributions that the Academy was expected to make under the current contributions set in accordance with the Fund's Funding Strategy Statement. After remittance in full, the outgoing Academy will have no further liability in the context of the Fund. Where the Group as a whole is in surplus (assessed at the most recent actuarial valuation) and representations are made by the outgoing body and accepted by the Administering Authority that an exit credit should be paid, then payment of such exit credit would fall due to the outgoing body. The payment would be calculated as the capitalised amount, as at the date of closure, of any future surplus adjustments that the outgoing body would benefit from under the amortisation period.

4.5 For Academies that chose not to participate within the Group under option 3.1.2, their termination contribution will be calculated in accordance with the Fund's Funding and Termination Policy which could result in a significantly different termination contribution being required.

4.6 The Administering Authority will explore all options at its disposal if the termination payment calculated under paragraph 4.4 is not forthcoming.

4.7 To the extent that any termination payment calculated under paragraph 4.4 is not forthcoming from the outgoing Academy or from any Guarantor or other form of security that was in place, the remainder of the Group will assume responsibility for any unrecovered deficit.

4.8 After the closure of an Academy, and either on the full remittance of any contribution required under paragraph 4.4 or the responsibility of the shortfall being transferred to the remaining Group under 4.7, full responsibility for any future pension fund risks associated with the now “orphan liabilities” (i.e. those relating to the outgoing Academy) will be borne by the remaining Group.

## SCHOOL/ACADEMY CONTRACTORS

4.9 As referenced in Appendix C, for any Admitted Body for whom the Scheme Employer is in the Schools/Academies pool, the contribution rate payable will be in line with the total contribution rate payable by the pool, as assessed as part of each triennial actuarial valuation. The Admitted Body then also becomes part of the pool.

4.10 For such Admitted Bodies, when their admission agreement ends a termination assessment will be performed in accordance with the Regulations. Any contribution payable to the Group (or exit credit payable from the Group) will be calculated by the Fund Actuary in a consistent manner to that set out in 4.4, other than that the period over which future deficit recovery contributions are capitalised (or surpluses are amortised) will be the **expected remainder of the contract length** (which will therefore be nil if the contract runs to its expected conclusion). After remittance in full, the outgoing Admitted Body will have no further liability in the context of the Fund. To the extent that any termination contribution calculated is not received from the Admitted Body, the responsibility for payment of the termination contribution will transfer to the original Scheme Employer within the pool.

## ACTUARIAL ASSESSMENT AND ACCOUNTING FOR PENSION COSTS

4.11 The contribution rates for all participating employers in the Fund are formally reassessed by the Fund Actuary every three years as part of an actuarial valuation exercise. As set out in paragraph 2.4, the contributions required for the Group as a whole will be assessed as if it were a single employer.

4.12 Even though pooled within the Group, it should be noted that Academies may still be required to report under the relevant Financial Reporting Standard (FRS) (depending on Department for Education guidelines).

4.13 Academies participating within the Group will have their individual funding position within the Group separately tracked for the purposes of their accounting requirements. If required, this can be actuarially assessed either at conversion, at the time the accounting figures are needed, or at the next triennial actuarial valuation of the Fund. The individual employer funding position / accounting figures, however, will not impact on the overall contributions due, as these will be calculated as described in paragraph 2.4.

## STATEMENT OF CONFIRMATION AND DEFAULT OPTION

4.14 All existing Academies Act 2010 Academies (who converted prior to 1 July 2012) were required to sign a formal statement of confirmation to their funding treatment (alongside Waltham Forest Council, as Administering Authority of the Fund). Nil returns were taken as the default choice of entering into the Group as set out in 3.1.1.

# APPENDIX E –

## GLOSSARY

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

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

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

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

**Best Estimate Assumption:** an assumption where the outcome has a 50/50 chance of being achieved.

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

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

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

**CPIH:** An alternative measure of CPI which includes owner occupiers’ housing costs and Council Tax (which are excluded from CPI).

**Covenant:** the assessed financial strength of the employer. A strong covenant indicates a greater ability (and willingness) to pay for pension obligations in the long run. A weaker covenant means that it appears that the employer may have difficulties meeting its pension obligations in full over the longer term or affordability constraints in the short term.

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

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

**Discount Rate:** the rate of interest used to convert a cash amount e.g. future benefit payments occurring in the future to a present value.

**Employer's Future Service Contribution Rate:** the contribution rate payable by an employer, expressed as a % of pensionable pay, as being sufficient to meet the cost of new benefits being accrued by active members in the future. The cost will be net of employee contributions and will include an allowance for the expected level of administrative expenses.

**Employing bodies:** any organisation that participates in the LGPS, including admission bodies and Fund employers.

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

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

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

**Fund / Scheme Employers:** employers that have the statutory right to participate in the LGPS. These organisations (set out in Part 1 of Schedule 2 of the 2013 Regulations) would not need to designate eligibility, unlike the Part 2 Fund Employers.

**Funding or solvency Level:** the ratio of the value of the Fund's assets and the value of the Fund's liabilities expressed as a percentage.

**Funding Strategy Statement:** this is a key governance document that outlines how the administering authority will manage employer's contributions and risks to the Fund.

**Government Actuary's Department (GAD):** the GAD is responsible for providing actuarial advice to public sector clients. GAD is a non-ministerial department of HM Treasury.

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

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

**Letting employer:** an employer that outsources part of its services/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.

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

**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.

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

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

**Minimum risk basis:** an approach where the discount rate used to assess the liabilities is determined based on the market yields of Government bond investments based on the appropriate duration of the liabilities being assessed. This is usually adopted when an employer is exiting the Fund.

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

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

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

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

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

**Present Value:** the value of projected benefit payments, discounted back to the valuation date.

**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.

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

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

**Real Return or Real Discount Rate:** a rate of return or discount rate net of (CPI) inflation.

**Recovery Plan:** a strategy by which an employer will make up a funding deficit over a specified period of time ("the recovery period"), as set out in the Funding Strategy Statement.

**Scheduled bodies:** types of employer explicitly defined in the LGPS Regulations, whose employers must be offered membership of their local LGPS Fund. These include Councils, colleges, universities, 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).

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

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

**Valuation funding basis:** the financial and demographic assumptions used to determine the employer's contribution requirements. The relevant discount rate used for valuing the present value of liabilities is consistent with an expected rate of return of the Fund's investments. This includes an expected out-performance over gilts in the long-term from other asset classes, held by the Fund.

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