St Edmundsbury
BOROUGH COUNCIL

B413

Cabinet
19 January 2011

Suffolk Pension Fund:
2010 Actuarial Valuation and Funding Strategy 2011–2013
(Feb11/12)

1. Summary and Reasons for Recommendations

1.1 The triennial valuation of the Suffolk Pension Fund (part of the Local Government Pension Scheme) took place in March 2010, and this report sets out the results of the valuation and the proposed course of action resulting from the increased funding deficit.

2. Recommendations

It is **RECOMMENDED** that:-

2.1 the Suffolk Pension Fund proposal to increase employer contributions by 1% each year for the next three years commencing 2011/2012 be approved, in line with projections already made in the Borough Council's Medium Term Financial Strategy; and

2.2 the outcome of the Hutton Report (due in the Summer of 2011) may have a significant impact on the entire structure of the pension fund and that a further report is brought back to Cabinet following the publication of this report.

3. Corporate Objectives

3.1 The recommendations meet the following contained within the Corporate Plan:-

(a) Corporate Priority: *'To raise Corporate standards and efficiency'*.

Contact Details	Portfolio Holder	Lead Officer
Name	John Griffiths	Liz Watts
Telephone	(01284) 757136	(01284) 757252
E-mail	john.griffiths@stedsbc.gov.uk	liz.watts@stedsbc.gov.uk

4. Key Issues

4.1 The Borough Council is part of the Suffolk County Council (SCC) administered Local Government Pension Scheme (LGPS), which has a formal actuarial valuation every three years.

4.2 The actuarial valuation is an assessment of the financial health of the pension fund and is undertaken by the SCC appointed actuary, Hymans Robertson.

4.3 The outcome of the valuation is a report on the funding level of the pension fund, which represents a comparison between the fund's assets (the value of its investments) and the fund's liabilities. The fund's liabilities are the present value of all the future pension payments that will fall to be paid, based on the service that has been accrued by scheme members up to the valuation date. The long-term objective of the pension fund is to maintain a 100% fully-funded position. The results of the actuarial valuation are used to determine the contributions to the pension fund which are required by the fund employers for the following three years.

4.4 The results of the actuarial valuation for the Suffolk Pension Fund at March 2010 show a deterioration in the funding level, from 89% funded at March 2007 to 82% funded at March 2010. The deficit on the pension fund has increased from £158 million at March 2007 to £306 million at March 2010.

	March 2007 £million	March 2010 £million
Liabilities	1,460	1,721
Market value of assets	1,302	1,415
Deficit (£m)	158	306
Pension Fund Funding level	89%	82%

4.5 The deficit for St Edmundsbury has increased from £1.46m at March 2007 to £15.8m at March 2010.

4.6 A summary of the factors which have affected the pension fund since the last triennial valuation in March 2007 is set out below.

4.7 **Investment performance**.
The investment returns over the three years to March 2010 have been significantly worse than the actuary's long-term expectations for the fund. The sharp falls in stock markets in 2007 and 2008 were followed by a partial recovery in 2009. However over the three years, the investment return for the fund was negative, -0.2% per year. This was the largest single factor in the deterioration of the funding level for the fund.

4.8 **Change in market conditions**.
The valuation of the fund's liabilities is based on the real return on fixed interest gilts. A decrease in the real yield on fixed interest gilts means an increase in the actuarial valuation of the fund's liabilities. Over the period since March 2007, there has been a decrease in the real yield on index-linked gilts. The actuary estimates that this factor has added around 10% to the fund's liabilities over the period.

4.9 **Mortality**.
The impact of mortality experience among pensioners over the valuation period has had an adverse effect on the fund, since fewer pensions in payment have ceased than expected by the actuary at the previous valuation. The actuary has also made allowance at the 2010 valuation for the expected future improvements in longevity, which increases

the cost to the fund of ongoing scheme membership.

4.10 **Change from RPI to CPI indexation**.
The announcement in the June 2010 Budget that the pensions in future will be subject to indexation in line with the consumer price index (CPI) rather than the retail price index (RPI) has reduced the actuary's assumption of long-term inflation for pension purposes by around 0.5% per year. The impact of this change is to improve the funding level, which in part offsets the adverse impact of the poor investment returns and the change in market conditions over the past three years.

4.11 **Salary growth**.
The level of pay growth between March 2007 and March 2010 was less than assumed by the actuary at the March 2007 valuation, which has had a positive effect on the actuarial valuation. The actuary has also allowed for the potential impact of a short-term reduction in pay increases in 2011 and 2012, in line with the Government's expectation of a pay freeze for public service workers earning more than £21,000 per year.

4.12 **Additional deficit contributions**.
The actuary determined employer contributions at the 2007 based on an expectation that the scheme deficit would be recovered over a period of around 15 years for the major public sector employers. The additional deficit contributions that have been made by employers over the period to 2010 have mitigated to some extent the adverse effect of the other changes over the inter-valuation period.

4.13 **Other factors**.
The actuary has allowed for the impact of the changes in the benefit and contribution structure of the scheme, following the introduction of the 'new-look' local government pension scheme at April 2008. The 'new-look' scheme was assessed as being broadly similar in overall cost to the pre-2008 scheme, although the impact on individual employers is likely to vary according to their actuarial position. There are a number of other smaller changes which have been broadly positive for the actuarial valuation.

4.14 The main changes that account for the movement in the funding deficit between March 2007 and March 2010 are summarised below.

	£million	**£million**
Deficit at March 2007		-158
Adverse effects		
Investment returns	-259	
Change in market conditions	-146	
Mortality changes	-15	-420
Positive effects		
Change from RPI to CPI	89	
Salary growth less than expected	85	
Additional employer contributions	41	
Other factors	57	272
Deficit at March 2010		**-306**

4.15 **Funding Strategy 2010**
The Funding Strategy sets out the Suffolk Pension Fund Committee's strategy to ensure that the pension fund will be fully funded over the long term. (The Council is represented on this SCC-run committee by Councillor John Hale). The Funding Strategy Statement has been developed on the basis of three broad principles:-

Prudence. The objective is to ensure the right balance between risk and reward in setting the funding and investment strategy of the fund, and in setting the individual employers' contributions to the fund.

Stability. The objective is to ensure, as far as possible, that employer contributions should not vary significantly from one valuation to the next.

Affordability. The objective is to recognise the potential impact of changes in employers' contributions on their overall budgets and resources, and to mitigate the adverse impact that any required changes might have, for example by the phasing of additional contributions, where this is feasible and prudent.

4.16 **Deficit Recovery Periods**

The Committee has agreed to adopt the following approach in setting employer contributions for individual scheme employers at the 2010 valuation. St Edmundsbury falls into the first category – 'Statutory bodies with tax raising powers'.

Type of Employer	**Maximum Length of Deficit Recovery Period**
Statutory bodies with tax raising powers	A period to be agreed with each employer not exceeding 20 years.
Transferee Admission Bodies	A period reflecting the remaining period of the contract.
Community Admission Bodies that are closed to new entrants	A period equivalent to the expected future working lifetime of the remaining scheme members allowing for expected leavers.
All other types of employer	A period to be agreed with each employer, not exceeding 15 years.

4.17 **Phasing in of Contribution Rises**

The Committee has agreed that any contribution increases that are required, based on the deficit recovery periods set out above, should be phased for statutory bodies with tax-raising powers over a period of up to six years, with a maximum increase each year equivalent to 1% of pay for the first three years. The proposal for St Edmundsbury is therefore that employer contribution rates increase from the current level of 16.6% in 2010/2011 to 19.6% in 2013/2014.

4.18 **Implementation**

The Pension Fund Committee has agreed to consult with scheme employers on the proposed Funding Strategy. The Pension Fund Committee will make a final decision on the Funding Strategy and the actuary will then certify the employer contributions for the three years from April 2011.

4.19 **The Hutton Independent Review**

Lord Hutton is chairing a review into public service pension provision and is due to publish his report in the Summer of 2011. The review has considered both the case for short-term savings and looked at how public service pensions can be made sustainable and affordable in the long term. The final report is likely to include recommendations for increasing employee contributions, as one of a range of solutions, to ensure that the future costs of pensions are adequately provided for in a manner which is both fair to public service workers and to the taxpayer.

5. Other Options considered

5.1 A number of funding strategies were proposed and considered by the Suffolk Pension Fund Committee.

6. Community impact *(including Section 17 of the Crime and Disorder Act 1998 and diversity issues)*

6.1 General

6.1.1 None.

7. Consultation

7.1 Corporate Management Team and Management Team.

8. Resource implications *(including asset management implications)*

8.1 Allowance has been made in the Medium Term Financial Strategy (MTFS) for a 1% increase per year over the next 6 years, in line with the proposals set out in this report.

9. Risk Assessment *(potential hazards or opportunities affecting corporate, service or project objectives)*

Risk area	**Inherent level of Risk** (before controls)	**Controls**	**Residual Risk** (after controls)
The Pension Fund is inadequately funded to make pension payments as they become due.	High	Actuarial advice has been sought and an agreed Funding Strategy formulated.	Medium
Contributions to the Pension Fund become disproportionately high for the council tax payer.	High	As above.	Medium
The LGPS is no longer sustainable as it currently stands.	High	The Hutton Inquiry is due to give its final report in Summer 2011 and is likely to recommend changes to secure the long term sustainability of the LGPS.	Medium

10. Legal or policy implications

10.1 As a local authority, the Borough Council is legally obliged to offer the LGPS to its staff. The Borough Council is bound by the Funding Strategy, once approved.

Wards affected	All	**Portfolio Holder**	Resources and Efficiency
Background Papers		**Subject Area** Finance	

W:\Democratic WP Services\Committee\Reports\Cabinet\2011\11.01.19\B413 Suffolk Pension Fund 2010 Actuarial Valuation & Funding Strategy 2011-2013.doc