

Pension Fund Panel

13 December 2018

Government Actuary Department (GAD) Section 13 Report

Report by Head of Investment, Risk and Commercial Finance - Resources

Purpose

To inform the Pension Panel of the outcome for the Royal Borough of Kingston Pension Fund in the GAD review of the actuarial valuations of LGPS Funds in England and Wales as at 31 March 2016.

Recommendation

The Pension Panel is recommended to note:

1. the content of this report.
2. RBK Pension Fund's performance in the GAD's assessment against four statutory measures: compliance, consistency, solvency and long-term cost efficiency.
3. the Fund actuary's presentation on RBK's Section 13 results.

Key Points

- A. RBK Pension Fund achieved mixed results in the first formal section 13 test on the actuarial valuations of all LGPS Funds by GAD under the Public Service Pensions Act 2013.
- B. RBK Pension Fund received Green Flags for three measures (compliance, consistency and solvency) and an Amber Flag for one (long-term cost efficiency).
- C. Under the regulations, GAD is required to report whether LGPS authorities satisfy four key aims: compliance, consistency, solvency and long-term cost efficiency. However, GAD has no statutory power to enforce actions on administering authorities or their advisers.

Context

1. Under section 13 of the Public Service Pension Act 2013, GAD is required to report on the extent to which LGPS administering authorities meet four statutory criteria. A 'dry run' was conducted by GAD based on the 2013 valuations and it published its test report in 2016.
2. The latest section 13 assessment is the first formal review by GAD and it is based on the actual valuations of all the LGPS Funds in England and Wales and supplementary information supplied by administering authorities and their actuaries.
3. On 27 September 2018, the Ministry of Housing, Communities and Local Government (MHCLG) published the inaugural GAD section 13 report on the

triennial actuarial valuations of the 91 LGPS Funds in England and Wales. The formal GAD section 13 report is appended to this report (Annex 1).

4. Under subsection (4) of section 13, GAD must report whether LGPS administering authorities' valuation approach meet the following prescribed aims:
 - Compliance: whether the valuation approach is compliant with the scheme regulations
 - Consistency: whether the valuation approach is consistent with methods used by other authorities
 - Solvency: whether the employer contribution rate is appropriate to ensure the solvency of the pension fund; and
 - Long-term cost efficiency: whether the employer contribution rate is appropriate to ensure the long-term cost efficiency of the pension fund and the scheme.
5. For each measure, a pension fund's score is "flagged" using a Red, Amber, Green (RAG) status to signal the pension fund's status for risks and issues from GAD's Perspective as follows:
 - Green Flag: No material issues to require a recommendation for remedial action vis-a-vis solvency or long-term cost efficiency
 - Amber Flag: Potential issue albeit not serious on its own to merit a recommendation for remedial action from a solvency or long-term cost efficiency perspective
 - Red Flag: Potentially material issue likely to warrant a recommendation for remedial action from a solvency or long-term cost efficiency perspective.
6. GAD uses Flags to determine whether further investigation is necessary. Administering authorities failing to meet one or more of the four statutory aims must take appropriate remedial steps per GAD's recommendation.
7. RBK Pension Fund received Green Flags in all but one measure in the 2016 GAD review.
 - Under long-term cost efficiency, RBK received an Amber Flag on the deficit reconciliation measure. From GAD's perspective, the Fund appears to have extended its deficit recovery end point by 2 years whilst reducing overall contributions by about 2%. Despite lengthy discussions between Hymans Robertson and GAD unfortunately, GAD could not be persuaded that the Fund's approach did not diminish the probability of the Fund being fully funded at the end of the recovery period.
 - Deficit recovery period is a relative measure in GAD's assessment. It is the period over which the Fund is expected to repay the deficit. On GAD's best estimate basis, it is assumed that deficit contributions are maintained at the current level. Consequently, for long-term efficiency measure, RBK scored 5.2 and ranked 90th out of 90. GAD considers that there is a potential risk but this by itself does not warrant a recommendation.
 - The Fund actuary believes that RBK adopted a robust approach in setting its long-term funding strategy. However, with the upcoming 2019 valuation in mind, the actuary has noted the drivers underlying the Amber Flag.
 - With regards to the solvency measure, RBK had a low Asset Shock (defined as the change in average employer contribution rates as a percentage of Core Spending Power of financing data after a 15% fall in value of return-seeking assets) level of 2.5% with scores ranging from surplus (the most resilient) to 7.4% (the least resilient). This measure shows the impact on total employer contribution

rates of a one-off decrease in the value of RBK's return-seeking assets as defensive assets are assumed to be unaffected.

- In their review, GAD used the SAB standardised funding level. RBK's local funding level (81.7%) was ranked mid-table but on the SAB restated standard basis, the funding level was 96.7% ranked towards the lower end of the upper segment of the table, indicating that the local fund basis is, relatively, more prudent than other Funds'
8. Some general highlights of the GAD section 13 report are:
- Nationally, the LGPS is in good financial health.
 - The market value of the LGPS total assets rose from £180bn in 2013 to £217bn in 2016.
 - The aggregate funding level of the LGPS improved from 79% in 2013 to 85% in 2016, due in part to better than expected returns on assets.
 - The LGPS received £6.9bn in employer contributions per annum on average of which about £2bn per annum was in respect of deficit recovery payments.
 - Of the 89 Funds tested, 70 (or 78.7%) received Green Flags on solvency and long-term cost efficiency measures. This compares favourably with 52 out of 90 Funds tested for the 2013 Dry Run exercise.
 - 20 Funds received Amber flags and 2 Funds got Red flags. At the 2013 test, there were 58 Amber flags and 5 Red flags.
9. In the section 13 report, GAD has made some recommendations to the Scheme Advisory Board as follows:
- That the SAB should push for a standardised approach to presentation of actuarial reports across the LGPS to promote greater transparency and support peer group comparison.
 - That the SAB should pursue better clarity and consistency in actuarial assumptions with limited scope for local discretion.
 - That the SAB should aim to secure parity in valuation approach for future academies.
 - That administering authorities should should review their funding strategy to ensure that the policy around surplus and deficits is consistent with CIPFA guidance. The deficit recovery plan should be on a continuous basis giving regard to actual fund experience.
10. The Fund actuary, Hymans Robertson, will be attending this Panel to give a presentation on the GAD Section 13 report to include:
- Background to the Section 13 review
 - An overview of RBK's Section 13 results from both the actuary's and GAD's perspective
 - A summary of the 2016 valuation approach
 - Feedback on Hymans Robertson's Section 13 experience and engagement with GAD; and
 - Insights on the 2019 valuation approach, including the actuary's thinking on the longer-term path of contributions for the Fund in light of the Section 13 results.

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Background papers

1. GAD Report, 27 September 2018 - Local Government Pension Scheme England and Wales: Review of the Actuarial valuations of Funds as at 31 March 2016 Pursuant to Section 13 of the Public Service Pensions Act 2013 - Executive Summary / Full Report / Report Appendices.