

Central Bedfordshire Council

AUDIT COMMITTEE

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Local Government Pension Scheme Update

Advising Officers: Director of Resources, Charles Warboys.
(charles.warboys@centralbedfordshire.gov.uk)

Head of Financial Control, Ralph Gould
(ralph.gould@centralbedfordshire.gov.uk)

Purpose of this report

1. To provide an update on the governance of the Local Government Pension Scheme (LGPS).

RECOMMENDATIONS

The Committee is asked to:

1. Consider and comment upon the issues raised within the report.

Overview and Scrutiny Comments/Recommendations

1. This report is for information only and has not been made to any Overview and Scrutiny Committee. Due to the significant values of assets and liabilities and the importance of the LGPS to the Council this Committee receives regular reports on the governance and performance of the Local Government Pension Scheme.

Background

2. The Local Government Pension Scheme (LGPS) in England and Wales is a funded public sector pension scheme with approximately 5.1 million members. The scheme, which currently invests some £240 Billion in assets, is the largest funded scheme in the UK and the fifth largest in the world.
3. The regulations for the scheme are determined by Parliament and developed by the Department of Communities and Local Government. The scheme is administered locally for participating employers by eighty nine funds across England and Wales.
4. The Bedfordshire Pension Fund, is administered by Bedford Borough Council, which is responsible for the pensions of Local Government employees across Bedfordshire, including Luton Borough Council and Central Bedfordshire Council.

5. Participation in the LGPS is open to public sector employers providing some form of service to the local community. Whilst the majority of members will be local authority employees (and ex-employees), the majority of participating employers are those providing services in place of (or alongside) local authority services such as academy schools, contractors, housing associations and charities.
6. At 31 March 2016 there were 145 active and 26 inactive scheme employers participating in the Bedfordshire LGPS. The actual Bedfordshire scheme membership numbers at March 2013 and 2016 are shown in Table 1 below. Following a number of years where active membership had declined, the introduction of auto enrolment (whereby the default position for new employees is that they are included in the scheme and have to opt out if they do not wish to be included), has contributed to an increase in active members for the Fund as a whole.

Table 1 LGPS Bedfordshire and CBC Membership at 31/3/13 and 31/3/16				
	Fund	Fund	CBC	CBC
	31 March 2013	31 March 2016	31 March 2013	31 March 2016
Active	17,442	20,428	3,948	4,753
Deferred	21,142	27,409	6,755	8,067
Pensioners	13,158	14,889	4,131	4,563
Total	51,742	62,726	14,834	17,383

Regulatory and Governance Changes

7. The creation of pooled investment vehicles for the England and Wales LGPS is progressing and eight pools have submitted business plans to the government. The various pools have been meeting with the Minister for State for Local Government and to date several pools have been advised to progress further with the implementation of their business plans including the Border to Coast Pension Partnership, of which the Bedfordshire Fund is a member.
8. The Enterprise Bill 2016 contains provisions to limit the value of exit payments an employee can receive from a public sector employer to £95,000. The exit payment cap includes actuarial strain costs which are those costs paid by the employer to the Pension Fund, and the Bill contains amendments to the LGPS Regulations so that members benefits can be amended to help meet the exit payment cap. The

arrangement is subject to implementation and DCLG are expected to conduct a consultation in the near future.

9. Relevant government Departments are also preparing further public sector exit payment reforms by the end of December 2016 for discussion with stakeholders. The government expects any reforms to be implemented by 30 June 2017.

Actuarial Valuation and Employer Contributions

10. Every three years, as required by the Regulations, the Actuary to the Fund calculates specific employer contribution rates. The 31 March 2016 actuarial valuation is now complete and contribution rates applying from 31 March 2017 have been confirmed. Any Pension Fund open to new members has an extremely long time horizon to consider when assessing its financial position and aiming for a fully funded position at a point in the future. Actuarial calculations inevitably rely on a series of assumptions and the Actuary adopts a risk modelling approach at individual employer level when setting employer contribution rates.
11. The actuarial valuation funding position is set out in Table 2 below. The Funding level in respect of the Council has remained unchanged since 2013 at 66% but the increase in liabilities and assets since that date has resulted in a £28.8m increase in the value of the deficit to £217.6m.

Table 2 – Council Actuarial Valuation Results		
	31 Mar 2013 £(M)	31 Mar 2016 £(M)
Past Service Liabilities		
Active Members (Final Salary)	148.5	130.1
Active Members (Career Average) from 1/4/14	-	35.1
Deferred pensioners	125.1	154.8
Pensioners	276.8	319.4
Total	550.3	639.4
Asset share	361.5	421.7
Deficit	(188.8)	(217.6)
Funding Level	66%	66%

12. Some of the assumptions made at the 2013 valuation compared to the actual experience are set out in table 3 below with the revised forward looking assumptions shown in the final column.

Table 3 – Actuarial Assumptions 2013 and 2016

	2013 Expected	Actual to 2016	Expected to 2019
Investment Returns 2013 - 16	15.4%	15.3%	12.8%
Salary increases p.a.	3.8%	2.7%	2.4%
Expected Pension increases p.a.	2.5%	1.3%	2.1%

13. The main contributions to the deficit increase relate to the change in financial assumptions (reduction in the discount rate from 4.9% to 4.1%) which has a financial impact of £37.2m and the interest on the existing deficit which amounted to £29m. The main positive impacts relate to the much lower than expected pension increases, £17m, and the impact of contributions paid above the cost of actual pension accrual, £13.4m. A reconciliation of the movement in the deficit is set out in table 4.

Table 4 – Movement in Council deficit 2013 – 2016

	£(M)	£(M)
Deficit at 31/3/13		(188.8)
Deficit increase		
Change in Financial assumptions	(37.2)	
Interest on deficit	(29.1)	
Pensioner mortality less than expected	(3.5)	
50:50 take up less than expected	(2.8)	
Investment returns less than expected	(0.4)	
Other experience items	(2.5)	
Total Deficit Increase items		(75.5)
Deficit Reduced		
Pension increases less than expected	17.0	
Contributions over cost of benefit accrual	13.4	
Change in mortality assumptions	6.3	
Salary increases less than expected	5.0	
Ill –health retirement strain	3.5	
Impact of Bulk transfers	1.1	
Other change and experience items	0.4	
Total Deficit reduction items		46.7
Deficit at 31/3/16		(217.6)

14. The cost of providing LGPS pension benefits depends on many factors including investment performance. To reflect the degree of uncertainty, employer contribution rates have been set by modelling the contributions required to fund the benefits under 5,000 different

economic scenarios. The employer contribution rates for the Council certified by the 2016 valuation and applying from 2017 along with the previous rates for information are set out in table 5 below.

Table 5 – CBC Certified Employer Contribution Rates			
Year	Future Current Service Rate % of pay	Lump Sum for deficit recovery £M	Total Rate %
2014/15	14.0	6.662	24.4
2015/16	14.0	7.212	24.9
2016/17	14.0	7.450	24.9
2017/18	16.9	5.903	24.2
2018/19	16.9	7.073	25.2
2020/21	16.9	8.296	26.5

15. The increase in the current cost of accrual (current service rate) from 14% of pay to 16.9% reflects the change in discount rate and the actual take up of the 50:50 membership option which has, in common with the LGPS as a whole, been much less than was originally assumed. The increase in contribution rates continues to be stabilised for the majority of public sector employers. The outcome of the initial modelling exercise suggested that the contributions would need to increase by more than the 0.5% p.a. steps that had applied in previous years. Further modelling took place to assess the appropriateness of a funding strategy for the councils assuming larger increases of +1% of pay p.a. The certified rates for the Council have been based on the later modelling results which generated an appropriate likelihood of achieving a fully funded position over a 20 year period.
16. There are two cost capping mechanisms in place for the LGPS which may lead to changes to the accrual rate or contribution rates from 2019. The caps only apply to future service costs and are independent of investment market conditions. Work on the two cost caps is already underway separately for the Scheme Advisory Board and HM Treasury.

Fund Management

17. The Fund has implemented an investment strategy and benchmark, linked to the Funds' liabilities, that seeks to provide less volatile returns compared to those Funds with a greater weighting to equities. At the Bedford Borough Council Pensions Committee meeting on 22nd November 2016 the Fund Administrator reported on the Pension Fund Performance to 30th September 2016. The market value of the Fund

and cash holdings as at 30th September 2016 was £1,922 million (Table 6) an increase of £194.5m since the 31 March 2016.

Table 6 Bedfordshire Fund Investment Asset classes and values at 30 September 2016			
Asset class	30 Sept-16	30 Sept-16	Bench mark
	£M	%	%
UK Equities	172.1	8.9	9
Overseas and Global Equities	822.4	42.8	41
Total Equities	994.5	51.7	50
Government Bonds	66.9		
Index Linked Gilts	111.1		
Absolute return Bonds	166.2		
Total Bonds	344.2	17.9	18
Property – (Indirect))	193.7	10.1	10
Multi Asset Absolute Return	328.2	17.1	20
Cash	61.3	3.2	2
Total Fund	1,921.9	100	100

18. The Fund's overall investment benchmark is a mixture of absolute and market returns and the absolute returns vary by manager e.g. RPI plus 5%, short term interest rates plus 4%. The managers invest in markets that can produce negative or flat returns and when this happens overall performance is likely to be negative relative to the specific benchmark and vice versa. Over 12 months to 30th September 2016 the overall benchmark was 9.6% and the strong equity market returns in recent months have resulted in a Fund investment performance of 16.4%.
19. Annualised 3 year returns were; Benchmark 6.7%, Fund 7.9% and annualised 5 years returns were; Benchmark 7.9% Fund 9.2%.
20. The main change in asset allocation to the reporting date has been a transfer of 9% of the Fund from UK equities to Global Equities.

Council Priorities

21. This report provides information about the Local Government Pension (LGPS). The LGPS has been subject to significant changes over recent years as central government strives to ensure that public sector pension schemes provide value for money. This objective is in line with the Council's own value for money priority.

Corporate Implications

Legal Implications

22. There are no specific legal implications as this report is made for information purposes. The LGPS in England and Wales is operated in line with various regulations made by the Secretary of State for Communities and Local Government in exercise of the powers conferred by the Superannuation Act 1972 and the Public Service Pensions Act 2013.

Financial and Risk Implications

23. There are no specific financial implications as this report is made for information purposes. The most recent Bedfordshire LGPS triennial actuarial valuation at 31 March 2016 disclosed Central Bedfordshire Council's liability of £639.4m (£550.3m 2013) compared to assets of £421.7m (£361.5m). It is planned to address the funding deficit of £217.6m (36%) over a twenty year period whilst stabilising the overall employer's contribution rate. In the last financial year 2015/16, employer contributions of 14% of pensionable pay were paid to the Bedfordshire Fund (approximately £8m p.a. including schools non-teaching staff) along with an additional lump sum of £7.212m towards the funding deficit.
24. LGPS contributions are a significant proportion of the Council's overall employment costs and as such the governance and performance of the scheme merits regular monitoring by this Committee.

Equalities Implications

25. There are no specific implications for equalities as this report is made for information purposes.

Conclusion and next Steps

26. The LGPS continues to be subject to considerable change and the current focus relates to the management of investments. The Fund and its employers also continue to address the operational issues arising from the implementation of the 2014 scheme for LGPS benefits.

27. The 2016 actuarial valuation has certified contribution rates having considered investment and funding strategies together and by modelling 5,000 future economic outcomes. As an exercise in risk management the use of stabilised contribution rates seeks to balance prudence with affordability. The pressures on overall affordability of the LGPS are recognised by the cost capping mechanisms which will be producing some initial results for consideration in the summer of 2017.

Appendices

None

Background Papers

None