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SOUTH YORKSHIRE
PENSIONS AUTHORITY

Authorised and regulated by the
Financial Conduct Authority

Diana Terris
Clerk

18 Regent Street
Barnsley
South Yorkshire
S70 2HG

www.southyorks.gov.uk

To: Members of the Pensions Authority
cc: Appropriate Officers

This matter is being dealt with by: Gill Richards Direct Line 01226 772806
Email: grichards@syjs.gov.uk

Dear Member

SOUTH YORKSHIRE PENSIONS AUTHORITY
4 OCTOBER 2018

Please find enclosed the item marked to follow on the above agenda: 'Item 20, Government Actuary's Department Section 13 Valuation'.

Yours sincerely

Gill Richards

Gill Richards
Democratic Services Officer

Encs

SOUTH YORKSHIRE PENSIONS AUTHORITY

10.00 AM AT THE MEETING ROOM 14, TOWN HALL, BARNSLEY, S70 2TA

AGENDA   Reports attached unless stated otherwise

SOUTH YORKSHIRE PENSIONS AUTHORITY

4 October 2018

Report of the Fund Director

THE GOVERNMENT ACTUARY'S 2016 SECTION 13 VALUATION OF THE LOCAL GOVERNMENT PENSION SCHEME

1) Purpose of the Report

To make members aware of the result of the Government Actuary's 2016 Section 13 Valuation of the Local Government Pension Scheme and highlight implications for the Authority.

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2) **Recommendations**

Members are recommended to note the contents of this report and the approach proposed by officers in the context of the 2019 Valuation.

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3) Background Information

3.1 The Public Sector Pensions Act 2013 requires (at section 13) that regular valuations of all the public sector pension schemes are undertaken to ensure that their costs remain within agreed parameters and that the schemes remain sustainable and demonstrate long term cost efficiency. For the Local Government Pension Scheme this activity is carried out by the Government Actuary alongside the local valuations (currently every 3 years). The Government Actuary (GAD) produces a report which effectively assesses whether any fund presents risks in terms of various "stress tests" and measures of long term cost efficiency. They also look closely at the actuarial assumptions adopted by funds and the individual actuarial firms.

3.2 GAD's report on their work related to the 2016 valuation has just been published and can be viewed at the link below, it has not been circulated with the papers due to the size of the document.

https://www.gov.uk/government/publications/local-government-pension-scheme-review-of-the-actuarial-valuations-of-funds-as-at-31-march-2016

3.3 GAD look at LGPS as a whole and the individual fund using four lenses

- *Compliance*: whether the fund's valuation is in accordance with the scheme regulations
- *Consistency*: whether the fund's valuation has been carried out in a way which is not inconsistent with the other fund valuations within LGPS
- *Solvency*: whether the rate of employer contributions is set at an appropriate level to ensure the solvency of the pension fund
- *Long term cost efficiency*: whether the rate of employer contributions is set at an appropriate level to ensure the long-term cost-efficiency of the scheme, so far as relating to the pension fund

3.4 The process throws up red and amber "flags" against funds which appear as outliers in any particular area.

3.5 In terms of compliance GAD conclude that the aims of s13 have been met in the local valuations. In particular they comment that more consistency in presentation and the definitions used in valuations has been achieved. They do, however, note issues with the quality of data in some cases and that 3 Administering Authorities (4 funds) failed to provide data in the required timescales.

3.6 In terms of consistency GAD makes a recommendation for the fund actuaries in terms of the presentation of disclosures within the valuation reports. In addition they note differences in assumptions within the local valuations relating to discount rate, mortality improvements, salary increases and commutation which do not appear to be based on local factors. They make a recommendation that the Scheme Advisory Board (SAB) look to achieve greater consistency in assumptions unless specifically justified by local factors, and also that SAB look to achieve a single consistent basis for future academy conversions.

3.7 In terms of solvency GAD note an overall improvement in funding levels but note issues in relation to a number of individual funds which either are furthest from full funding or are potentially at risk in a stress situation. In this latter area South Yorkshire is one of four funds flagged as amber, an issue dealt with later in this report.

3.8 In terms of long term cost efficiency GAD note the overall improvement in funding levels, but highlight some funds which have extended their deficit recovery periods and recommend that funds review their funding strategy statements to ensure that the treatments of surpluses/deficits are fair to both current and future taxpayers.

3.9 Overall the GAD report does not contain any real surprises. The areas where they highlight differences in practice between the four actuarial firms have been known for some time, and there is risk as well as benefit to funds in the greater standardisation of actuarial approach GAD appear to be seeking. Greater transparency around assumptions is, however, a good thing in and of itself encouraging debate around the appropriateness of individual assumptions in the local context. A good example of this is in relation to commutation where the information provided in the GAD review will enable a discussion with the actuary about the significant difference between the assumption and local reality.

3.10 The area where South Yorkshire has received a flag is in relation to an asset shock test. This test is designed to examine whether employers in the Fund would be able to deal with the contribution rate impact of a significant downturn in the markets. To determine the “affordability” of additional contributions GAD look at the “core spending power” of the statutory employer within the Fund. In fairness to GAD there is no other easily available measure which they could use for a test of this sort, but it does mean that there are fundamental flaws in the test. For example not all statutory employers have “core spending power “measures and some elements of the contributions from statutory employers are outside core spending power (for example Housing Revenue Account staff in the District Councils).

3.11 GAD determined that they would flag funds where an asset shock would result in a contribution increase for statutory employers of 3% or more of core spending power. Four funds were flagged in this way, of which one was the LPFA which because it has no council within the Fund had to be tested in a somewhat different way. The three more conventional funds flagged were:

- South Yorkshire
- Tyne and Wear
- West Yorkshire

3.12 In addition to this Merseyside was just below the 3% threshold. Members will note that these three funds and Merseyside all serve northern metropolitan areas which have been disproportionately impacted by the reductions in central government support for local authorities since 2010, which perhaps highlights the limitations of the data used in this test. Officers anticipate that there may be some collaboration between funds to assist GAD in developing a more suitable test for future exercises.

3.13 From a more parochial local point of view SYPA put in place its equity protection strategy in consultation with the statutory employers precisely to protect the fund against the sort of shock which GAD is testing in this case. Officers have made this point to GAD as part of the discussions they have undertaken with funds who have received a flag and consequently GAD have acknowledged this in their report in positive terms. However, GAD’s view is that the implementation of the equity protection strategy was too late to impact this section 13 exercise. Officers will continue to engage with GAD to demonstrate that the impact of the equity protection strategy has been to negate the risk they have highlighted.

3.14 The general tenor of GAD's report seems to be toward a much more prescriptive valuation basis, allowing less ability to reflect local factors. Key elements of this are opposed by the four actuarial firms, although it is clear that between 2013 and 2016 there was a greater standardisation of approach between the firms. From SYPA's point of view any valuation basis needs to strike a balance between the prudence of the approach and the ability of employers to pay any given level of contributions. Achieving this requires there to be some safety valves in the valuation process which may be removed through greater standardisation and centralisation of the process. The nature of the scrutiny placed on the local valuation process through this review also adds a further range of considerations into the local valuation process in terms of anticipating how GAD will view specific decisions made locally.

4) Implications and risks

- Financial – There are no direct financial implications arising from this report.
- Legal – No implications have been identified.
- Diversity – No implications have been identified.
- Risk – The results of the GAD process present a number of challenges for the Authority. Clearly receiving a flag, however qualified, as a result of the process presents reputational risks which will need to be managed. However, perhaps more significantly the framework created by GAD presents a series of new considerations that will need to be addressed with the Actuary as part of the 2019 valuation process which depending on how the different considerations are weighed may make it more difficult to achieve results that are acceptable to all stakeholders.

George Graham
Fund Director

01226 772887
ggraham@sypa.org.uk

Background papers used in the preparation of this report are available for inspection at the offices of the Authority in Barnsley.