SOUTH YORKSHIRE
PENSIONS AUTHORITY

Subject	**Funding Strategy Statement**	**Status**	For Publication
Report to	Authority	**Date**	23 January 2020
Report of	Fund Director		
Equality Impact Assessment	Not Required	Attached	No
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1 Purpose of the Report

To consider and approve the Authority's Funding Strategy Statement following consultation with stakeholders and the completion of the valuation process.

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2 Recommendations

2.1 Members are recommended to:

a. **Note the process of engagement undertaken around the valuation results and the Funding Strategy Statement.**

b. **Note the comments made by stakeholders in relation to the draft Funding Strategy Statement and consider the proposed response to those comments.**

c. **Approve the Funding Strategy Statement at Appendix A.**

d. **To delegate to the Fund Director in consultation with the Actuary authority to finalise the Rates and Adjustments Certificate in line with the statutory timetable.**

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3 Link to Corporate Objectives

3.1 This report links to the delivery of the following corporate objectives:

Listening to our stakeholders

To ensure that stakeholders' views are heard within our decision making processes.

The Authority is required to consult with stakeholders in preparing the Funding Strategy Statement (FSS). This report demonstrates a clear link between the comments made by stakeholders and the final FSS.

Investment Returns

To maintain an investment strategy which delivers the best financial return, commensurate with appropriate levels of risk, to ensure that the Fund can meet both its immediate and long term liabilities.

The FSS is, in effect the vehicle for setting out the Authority's strategy for setting employer contribution rates, and is therefore both influenced by and influences the Authority's investment strategy.

Effective and Transparent Governance

To uphold effective governance showing prudence and propriety at all times.

The way in which the Authority engages with stakeholders around the valuation process and the development of the FSS is important in building the confidence of the employer community in the way in which the Authority exercised its responsibilities for stewardship of the Fund while balancing the different interests involved.

4 Implications for the Corporate Risk Register

4.1 The actions outlined in this report address a number of key risks facing the Authority, in particular those relating to the maintenance and improvement of the funding level, risks around employer default and risks around cash flow. By setting and adhering to clear policies in these areas which are set out in the FSS the Authority is able to manage these risks in an appropriate way that balances the various interests involved.

5 Background and Options

5.1 The culmination of each triennial valuation process is the approval of the revised Funding Strategy Statement (FSS) together with the signing off of the Rates and Adjustments Certificate by the actuary. This report brings the valuation process to a conclusion for members by presenting the final FSS for approval.

5.2 The purpose of the FSS is to lay out both the assumptions used to underpin the valuation process but also a range of policies about how contribution rates are set given the overarching objective to achieve longer term stability in contributions. As a statutory document it is a requirement that the Authority consults with stakeholders on the policies which it proposes to implement. The Consultation process in this cycle has involved the following:-

- A formal consultation with all employers on key actuarial assumptions before the valuation date of 31st March 2019.
- A presentation by the Actuary at the Employers' Forum on 12th November 2019.
- Discussions with key employer groups covering both valuation results and these policy issues (separate meetings were held with District Councils, Academies (5 sessions were provided for Academies), F&HE Institutions and other employers).
- All employers have been provided with the draft Funding Strategy Statement for comment.
- The Local Pension Board considered the draft FSS at its December meeting.

5.3 The feedback from this process of engagement is reflected below. It should be noted that this is a more active process of engagement with employers than has previously been undertaken.

5.4 The key changes reflected in the draft FSS which is at Appendix A are set out below:

- **Alternative Funding Targets –** As a precursor to the introduction a differentiated investment strategies reflecting the risk to the Fund posed by specific employers different funding targets may be used for employers with a lesser covenant in order to provide more certainty that liabilities will be met. This approach will initially be particularly focussed on Community Admission Bodies especially those without a guarantor.
- **McCloud –** An estimate has been made of the impact of the McCloud case and employers are being provided with the option of making additional contributions now to begin to meet the cost or to make what may be a greater level of contributions (including a "backdating" element) once the final remedy is known. This potentially provides greater stability in contribution rates for employers who choose take this option.
- **Short Term Pay Growth –** The assumption about short term pay growth based on research with major employers has been set at 3% for the next 3 years. This includes the effect of incremental progression as well as headline pay awards and thus is likely to be closer to the real growth in the pay bill.
- **Ill Health Captive –** The scope of this arrangement which in effect insures ill health liabilities for smaller employers will be increased to all employers with fewer than 100 active members. Employers who have participated up to now will likely see a reduction in premiums due to experience over the last 3 years.
- **Prepayments –** Options will be provided for all employers to prepay any deficit contributions, in addition the option to pay off the whole deficit will be offered. District Councils will continue to be offered a prepayment arrangement in relation to future service contributions.
- **Contribution Stability –** For employers who still have a deficit the total cash level of contributions over the period 2020-23 will be maintained at the same level as currently plus inflation. This provides a balance in sharing the benefits of improved funding levels between employers and the Fund where a deficit remains while increasing the certainty of recovering the deficit.
- **Deficit Recovery –** The maximum deficit recovery period will be 16 years (a reduction of 3 years as compared to the last valuation). Where possible and within the overall approach to contribution stability deficit recovery periods for individual employers will be brought down further.
- **Phasing of Contribution Increases –** Phasing of contribution increases will be allowed (at the discretion of the Fund) but only on the basis of the total contributions payable over the period 2020-23 being the same as required in the actuary's initial assessment. Additionally discussions are being held with Academies and F&HE Institutions about implementing any new contribution plans on an academic year basis in line with funding.
- **Academies –** The Fund's default position will be that Multi Academy Trusts are treated as a single employer, although individual schools will continue to be tracked separately.
- **Outsourcing and Exits –** Policies are proposed to address issues surrounding exit credits, the new fair deal and the Government's proposals around deferred employer status.

5.5 The framework set out in the draft FSS is intended to protect the Fund and ensure the greatest possible likelihood of achieving and maintaining full funding at employer level while at the same time giving flexibility to recognise both the general financial pressures facing employers and deal with cases of particular difficulty.

5.6 There are a number of uncertainties which the policy framework set out in the draft FSS seeks to address. The largest of these relates to the impact of the McCloud judgement, where while an estimate of the cost has been made no proposals have been tabled by the Government which would define the nature of the actual remedy. In general terms it will, all other things being equal, serve employers better to make provision for these costs now, rather than wait until a remedy is in place and play catch up. However, there is an affordability argument and the Fund has no power to make employers pay additional contributions in relation to what is at present a notional liability.

5.7 A limited number of comments have been received from stakeholders as follows:

- The Local Pension Board noted the FSS and made no specific comments on its content.
- Two Community Admission Bodies with no guarantor have raised specific circumstances with regard to their own treatment under the alternative funding targets arrangements and the arrangements for contribution stability. These will be dealt with through individual discussion, as in essence both are asking the Authority to exercise discretion in the application of the policy. However, fundamentally the policy intent is to reduce the risk of employer default impacting on the rest of the Fund and of deficits recurring once they have been eliminated both of which are fundamental to the prudent management of the Fund.
- Two Multi Academy Trust have responded in relation to their own preferences in regard to the implementation date for contribution changes and the use of a single rate for a MAT. These views will be reflected in the finalisation of the rates and adjustments certificate as they do not impact on the principles in either case.
- One College queried the grouping of Academies and F&HE Institutions for the purposes of employer risk management. While the scale and nature of funding of these institutions does differ significantly at present officers' view is that the level of risk to the Fund from these different types of institutions is broadly similar and therefore grouping them together for this purpose, which will ultimately include the development of a differentiated investment strategy is appropriate. However, the final assessment of the risk posed by any individual employer is an individual judgement and a result of discussion with that employer therefore these groupings are more of an administrative convenience than fixed entities.

5.8 Alongside the consultation on the FSS officers and the Fund's Actuary have been discussing proposed contribution rates with employers in order to finalise the actuary's report and the Rates and Adjustments Certificate which is the document which summarises the contributions to be paid by all employers. Overall the result of the valuation point to a funding level of 99.2% with a residual net deficit of some £68m. However, the results and thus the implications for contributions vary significantly between, and within groups of employers. In general employers who have been very long term participants in the Fund are either now in or very close to a surplus position. Thus the removal or reduction of their deficit contributions more than meets any McCloud liability allowing them to make savings. On the other hand schools who have more recently converted to academies have received less benefit from the compounding of investment returns over time and therefore have not seen the same degree of closure in their deficit as other employers.

5.9 Given the timescale for agreeing final contribution rates with all employers and the need to ensure publication of the final actuarial report it is suggested that as this is an essentially technical exercise of applying the policies set out in the FSS that the agreement of contribution rates and finalisation of the Rates and Adjustments Certificate is delegated to the Fund Director in consultation with the actuary. A report summarising the impact of the valuation process on contribution levels will be brought to a future meeting.

6 Implications

6.1 The proposals outlined in this report have the following implications:

Financial	The FSS defines the plan for contributions over the next valuation period and consequently has significant implications for the Fund's cash flow and the balance between contribution income and benefit payments. As such, given the change in funding level, there are potentially significant implications for the financial balance within the Fund and the need to utilise, rather than reinvest, investment income. These implications will be addressed in the Investment Strategy review and the update of the Medium Term Financial Strategy.
Human Resources	None
ICT	None
Legal	The production of the FSS including consultation on its proposed contents is a requirement of the Local Government Pension Scheme regulations.
Procurement	None

George Graham

Fund Director

Background Papers	
Document	**Place of Inspection**