

RHONDDA CYNON TAF COUNTY BOROUGH COUNCIL PENSION FUND

FUNDING STRATEGY STATEMENT

March 2021



Rhondda Cynon Taf County Borough Council Pension Fund

Funding Strategy Statement

SECTION 1

Introduction

Overview

This Statement has been prepared in accordance with Regulation 58 of the Local Government Pension Scheme Regulations 2013 (as amended) (the LGPS Regulations). The Statement describes Rhondda Cynon Taf County Borough Council's strategy, in its capacity as Administering Authority (the Administering Authority), for the funding of the Rhondda Cynon Taf County Borough Council Pension Fund (the Fund).

As required by Administration Regulation 58(3), the Statement has been reviewed (and where appropriate revised) having regard to guidance published by CIPFA in September 2016 as well as the supplementary statutory guidance issued by MHCLG: Guidance on Preparing and Maintaining Policies on Review of Employer Contributions, Employer Exit Payments and Deferred Debt Agreements.

Consultation

In accordance with Regulation 58(3), officers, elected members, and representatives of all employers participating within the Rhondda Cynon Taf County Borough Council Pension Fund, have been consulted on the contents of this Statement and their views have been taken into account in formulating the Statement. However, the Statement describes a single strategy for the Fund as a whole.

In addition, the Administering Authority has had regard to the Fund's Investment Strategy Statement published under Regulation 7 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 (the Investment Regulations) and the Scheme Advisory Board's Guide to Employer Flexibilities.

The Fund Actuary, Aon Solutions UK Ltd, has also been consulted on the contents of this Statement.

Policy Purpose

The purpose of this Funding Strategy Statement is to document the process by which the Administering Authority:

- establishes a clear and transparent strategy, specific to the Fund, which will identify how employer's pension liabilities are best met going forward
- supports the regulatory requirement in relation to the desirability of maintaining as nearly constant a primary contribution rate as possible
- enables overall employer contributions to be kept as constant as possible and (subject to the Administering Authority not taking undue risks and ensuring that the regulatory requirements are met) at reasonable cost to the taxpayers, scheduled, designating, and admitted bodies
- ensures that the regulatory requirements to set contributions so as to ensure the solvency and long-term cost efficiency of the Fund are met
- takes a prudent longer-term view of funding the Fund's liabilities.

Noting that whilst the funding strategy applicable to individual employers or categories of employers must be reflected in the Funding Strategy Statement, its focus should at all times be on those actions which are in the best long-term interests of the Fund.

Links to investment policy set out in the Investment Strategy Statement

The Authority has produced this Funding Strategy Statement having taken an overall view of the level of risk inherent in the investment policy set out in the Investment Strategy Statement and the funding policy set out in this Statement. The Authority accepts that the outcome of formulating a strategic asset allocation needs to be consistent with achieving the solvency and deficit recovery targets and meeting obligations when they fall due.

Fixed interest and index-linked Government bonds are considered to provide an effectively guaranteed return if held to redemption (assuming the Government doesn't default). The Fund's asset allocation as set out in the Investment Strategy Statement invests a significant proportion of the Fund in assets such as equities which are expected but not guaranteed to produce higher returns than Government bonds in the long term. The Administering Authority has agreed with the Fund Actuary that the funding target on the ongoing basis will be set by explicitly considering the expected return on the assets. The Administering Authority recognises that future investment returns are not guaranteed and that, in the absence of any other effects, if the expected returns are

not achieved the solvency position of the Fund will deteriorate.

The funding strategy recognises the investment targets and the inherent volatility arising from the investment strategy, by being based on financial assumptions which take account of the expected average return, and by including measures which can be used to smooth out the impact of such volatility.

The Administering Authority will continue to review both documents to ensure that the overall risk profile remains appropriate including, where appropriate, use of asset liability modelling or other analysis techniques.

Review of this Statement

The Administering Authority undertook its latest substantive review of this Statement in March 2021.

The Administering Authority will formally review this Statement as part of the triennial valuation as at 31 March 2022 unless circumstances arise which require earlier action.

The Administering Authority will monitor the funding position of the Fund on an approximate basis at regular intervals between valuations, and will discuss with the Fund Actuary whether any significant changes have arisen that require action.

SECTION 2

Aims and Purpose of the Fund

Purpose of the Fund

The purpose of the Fund is to invest monies in respect of contributions, transfer values and investment income to produce a Fund to pay Scheme benefits over the long term and in so doing to smooth out the contributions required from employers over the long term.

The Aims of the Fund

The main aims of the Fund are:

- 1. To comply with regulation 62 of the Local Government Pension Scheme Regulations 2013 and specifically to adequately fund benefits to secure the Fund's solvency while taking account of the desirability of maintaining as nearly constant a primary employer contribution rate as possible. The Fund should achieve and maintain solvency and long term cost efficiency (subject to the administering authority not taking undue risks), which should be assessed in light of the risk profile of the fund and the risk appetite of the administering authority and employers alike, at reasonable cost to the taxpayers, scheduled, resolution and admitted bodies.**

The Administering Authority recognises that the requirement to keep employer primary contribution rates as nearly constant as possible can run counter to the following requirements:

- the regulatory requirement to secure solvency and long term cost efficiency,
- the requirement that the costs should be reasonable, and
- maximising income from investments within reasonable cost parameters (see later)

Producing low volatility in employer contribution rates requires material investment in assets, which 'match' the employer's liabilities. In this context, 'match' means assets that behave in a similar manner to the liabilities as economic conditions alter. For the liabilities represented by benefits payable by the Local Government Pension Scheme should there be no employers to fund the liabilities in the future, such assets would tend to comprise gilt edged investments.

Other classes of assets, such as stocks and property, are perceived to offer higher long-term rates of return, on

average, and consistent with the requirement to maximise the returns from investments the Administering Authority invests a substantial proportion of the Fund in such assets. However, these assets are more risky in nature, and that risk can manifest itself in volatile returns over short-term periods.

This short-term volatility in investment returns can produce a consequent volatility in the measured funding position of the Fund at successive valuations, with knock on effects on employer contribution rates. The impact on employer rates is mitigated by use of a risk-based approach to setting the investment return assumption; a smoothing mechanism which recognises the statutory nature of the Fund and its largest employers.

The Administering Authority recognises that there is a balance to be struck between the investment policy adopted, the smoothing mechanisms used at valuations, and the resultant smoothness of employer contribution rates from one valuation period to the next.

The Administering Authority also recognises that the position is potentially more volatile for Admission Bodies with short-term contracts where utilisation of smoothing mechanisms is less appropriate.

2. To ensure that sufficient resources are available to meet all liabilities as they fall due.

The Administering Authority recognises the need to ensure that the Fund has, at all times, sufficient liquid assets to be able to pay pensions, transfer values, costs, charges and other expenses. It is the Administering Authority's policy that such expenditure is met, in the first instance, from incoming employer and employee contributions to avoid the expense of disinvesting assets. The Administering Authority monitors the position on a monthly basis to ensure that all cash requirements can be met.

3. To manage employers' liabilities effectively.

The Administering Authority seeks to ensure that all employers' liabilities are managed effectively. In a funding context, this is achieved by seeking regular actuarial advice, ensuring that employers, Committee and Board members are properly informed, and through regular monitoring of the funding position.

4. To maximise the income from investments within reasonable risk parameters.

The Administering Authority recognises the desirability of maximising investment income within reasonable risk parameters. Investment returns higher than those available on government stocks are sought through investment in other asset classes such as stocks and property. The Administering Authority ensures that risk parameters are reasonable by:

- restricting investments to the maximum percentages set out in the Investment Strategy Statement.
 - restricting investment to asset classes generally recognised as appropriate for UK pension funds.
 - analysing the potential risk represented by those asset classes in collaboration with the Fund's Actuary, Investment Advisors, Fund Managers and the Wales Pension Partnership.
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SECTION 3

Responsibilities of the Key Parties

Responsibilities of the key parties The three parties whose responsibilities to the Fund are of particular relevance are the Administering Authority, the Individual Employers and the Fund Actuary.

Their key responsibilities are set out below:

Administering Authority

The Administering Authority's key responsibilities are:

- 1. To operate the pension fund**
- 2. Collecting employer and employee contributions, investment income and other amounts due to the Fund as stipulated in LGPS regulations and, as far as the Administering Authority is able to, ensure these contributions are paid by the due date.**

Individual employers must pay contributions in accordance with Regulations 67 to 71 of the Regulations. The Administering Authority will ensure that all employers are aware of these requirements especially the requirement of the Pensions Act 1995 that members' contributions are paid by the 19th of the month following the month that it is paid by the member. The Administering Authority may charge interest on late contributions in accordance with Regulation 71 of the Regulations.

The Administering Authority will ensure that action is taken to recover assets from employers who have exited the Fund by

- requesting that the Fund Actuary calculates the deficit at the date of exit of the employer
- notifying the employer that it must meet any deficit calculated in the exit valuation.

- 3. Pay from the Fund the relevant entitlements as stipulated by LGPS Regulations.**
- 4. Invest surplus monies in accordance with the LGPS regulations.**

The Administering Authority will comply with Regulation 7(8) of the Investment Regulations.

- 5. Ensure that cash is available to meet liabilities as and when they fall due.**

The Administering Authority recognises this duty and discharges it in the manner set out in the Aims of the Fund above.

6. Manage the valuation process in consultation with the Fund's actuary

The Administering Authority ensures it communicates effectively with the Fund Actuary to:

- agree timescales for the provision of information and provision of valuation results
- ensure provision of data of suitable accuracy
- ensure that the Fund Actuary is clear about the Funding Strategy Statement
- ensure that participating employers receive appropriate communication throughout the process
- ensure that reports are made available as required by Guidance and Regulation
- enable the Pension Committee and Board to review the valuation progress
- ensure information is provided to the Government Actuary's Department to enable it to discharge its functions under Section 13 of the Public Service Pensions Act 2013 and as Scheme Actuary

7. Prepare and maintain an Investment Strategy Statement and a Funding Strategy Statement after due consultation with interested parties.

The Administering Authority will ensure that both documents are prepared and maintained in the required manner.

8. Monitor all aspects of the Fund's performance and funding and amend these two documents as required.

The Administering Authority monitors the investment performance and funding position of the Fund on a quarterly basis. The Investment Strategy Statement will be formally reviewed annually, and the Funding Strategy Statement every three years as part of the valuation cycle, unless circumstances dictate earlier amendment.

9. Effectively manage any potential conflicts of interest arising from its dual role as both Administering Authority and Scheme Employer.

10. Ensure consistent use of policies relating to revising employer contributions between formal

valuations, entering into deferred debt arrangements and spreading exit payments and that the process of applying those policies is clear and transparent to all fund employers.

Individual Employers

Individual Employers will:

- Deduct contributions from employees' pay.
 - Pay all ongoing contributions, including their employer contributions and contributions due under a Deferred Debt Agreement as determined by the Fund Actuary, promptly by the due date.
 - Develop a policy on certain discretions and exercise discretions within the regulatory framework.
 - Pay for added years in accordance with agreed arrangements.
 - Notify the Administering Authority promptly of all changes to membership, or other changes which affect future funding, including any notifiable events as set out in the Pensions Administration Strategy.
 - Pay any exit payments required in the event of their ceasing participation in the Fund.
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The Fund Actuary

The Fund Actuary will:

- prepare valuations including the setting of employers' contribution rates at a level to ensure solvency and long term cost efficiency after agreeing assumptions with the Administering Authority and having regard to the Funding Strategy Statement and the Regulations.
- prepare advice and calculations in connection with bulk transfers and the funding aspects of individual benefit-related matters.
- provide advice and valuations on the exit of fund employers.
- provide advice to the Administering Authority on bonds and other forms of security against the financial effect on the Fund of Employer's default
- assist the Administering Authority in assessing whether employer contributions need to be revised between valuations as permitted or required by the regulations, in particular in relation to any review of contributions between triennial valuations under Regulations 64(4) and 64A

- provide advice as required to support the Administering Authority in deciding whether or not to put in place a Deferred Debt Agreement under Regulation 64(7A) or spread an exit payment under Regulation 64B
 - ensure that the Administering Authority is aware of any professional guidance or other professional requirements which may be of relevance to his role in advising the Fund.
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SECTION 4

Funding Target, Solvency, Long Term Cost Efficiency and Notional Sub-Funds

Funding Principle The Fund is financed on the principle that it seeks to provide funds sufficient to enable payment of 100% of the benefits promised.

Funding Targets and assumptions regarding future investment strategy

The Funding Target is the amount of assets which the Fund needs to hold at any point in time such that the funds held, plus future anticipated investment returns on those funds, and taking into account the anticipated future experience of the membership and contributions due from the membership, meet the funding principle.

Some comments on the principles used to derive the Funding Target for different bodies in the Fund are set out below.

Scheduled Bodies and certain other bodies

The Administering Authority will adopt a general approach in this regard of assuming indefinite investment in a broad range of assets of higher risk than low risk assets for Scheduled Bodies and certain other bodies which are, or can be treated as if they are long term in nature.

The Administering Authority adopts a risk based approach to funding. In particular the discount rate (for most employers) has been set on the basis of the assessed likelihood of meeting the funding objectives. The Administering Authority has considered 3 key decisions in setting the discount rate:

The long-term Solvency Target (i.e. the funding objective – where the Administering Authority wants the Fund to get to);

The Trajectory Period (how quickly the Administering Authority wants the Fund to get there); and

The Probability of Funding Success (how likely the Administering Authority wants it to be now that the Fund will actually achieve the Solvency Target by the end of the Trajectory Period).

These three choices, supported by complex (stochastic) risk modelling carried out by the Fund Actuary, define the discount rate (investment return assumption) to be adopted and, by extension, the appropriate levels of employer contribution payable. Together they measure the riskiness (and hence also the degree of prudence) of

the funding strategy. These are considered in more detail below.

Admission Bodies and bodies closed to new entrants

For Admission Bodies the Administering Authority will have specific regard to the potential for participation to cease (or to have no contributing members), the potential timing of exit from the fund, and any likely change in notional or actual investment strategy as regards the assets held in respect of the Admission Body's liabilities at the date of cessation (i.e. whether the liabilities will become 'orphaned' or whether a guarantor exists to subsume the notional assets and liabilities).

Orphan liabilities

These are liabilities with no access to funding from any employer in the Fund. To minimise the risk to other employers in the Fund the assets notionally related to these liabilities will be assumed to be invested in low risk investments. This is described in more detail later in this document.

Solvency and 'Funding Success'

The Fund's primary aim is long-term solvency. Accordingly, employers' contributions will be set to ensure that 100% of the liabilities can be met over the long term.

The Fund is deemed to be solvent when the assets held are equal to or greater than 100% of the liabilities assessed using appropriate actuarial methods and assumptions. The Administering Authority believes that its funding strategy will ensure the solvency of the Fund because employers collectively have the financial capacity to increase employer contributions should future circumstances require, in order to continue to target a funding level of 100%.

For Scheduled Bodies and Admission Bodies where a Scheme Employer of sound covenant has agreed to subsume its assets and liabilities following cessation, the Solvency Target is set :

- at a level advised by the Fund Actuary as a prudent long-term funding objective for the Fund to achieve at the end of the Trajectory Period,
- based on continued investment in a mix of growth and matching assets intended to deliver an overall return above the rate of increases to pensions and pensions accounts (Consumer Price Index (CPI)).

As at 31 March 2019 the long-term rate of CPI is assumed to be 2% p.a. and a prudent long-term investment return of 2%

above CPI is assumed. As at 31 March 2019 the solvency discount rate is therefore 4% p.a.

For Admission Bodies and other bodies whose liabilities are expected to be orphaned following cessation, a more prudent approach will be taken. The Solvency Target will be set by considering the valuation basis which would be adopted should the body leave the Fund. For most such bodies, the Solvency Target will be set commensurate with assumed investment in an appropriate portfolio of Government bonds after cessation.

For deferred employers it is expected that the Solvency Target will be set by considering the valuation basis which would be adopted once the Deferred Debt Agreement (DDA) ends. For most such bodies, the Solvency Target will be set commensurate with assumed investment in Government bonds at the end of the period of the DDA.

Probability of Funding Success

The Administering Authority considers funding success to have been achieved if the Fund, at the end of the Trajectory Period, has achieved the Solvency Target. The Probability of Funding Success is the assessed chance of this happening based on the level of contributions payable by members and employers and asset-liability modelling carried out by the Fund Actuary.

The discount rate, and hence the overall required level of employer contributions, has been set such that the Fund Actuary estimates there is around a 75% chance that the Fund would reach or exceed its Solvency Target after 25 years.

Funding Target

The Funding Target is the amount of assets which the Fund needs to hold at the valuation date to pay the liabilities at that date as indicated by the chosen valuation method and assumptions and the valuation data. The valuation calculations, including future service contributions and any adjustment for surplus or deficiency set the level of contributions payable and dictate the chance of achieving the Solvency Target at the end of the Trajectory Period (defined below). The key assumptions used for assessing the Funding Target are summarised in Appendix 1.

Consistent with the aim of enabling the primary rate of employers' contributions to be kept as nearly constant as possible, contributions are set by use of the Projected Unit valuation method for most employers. The Projected Unit method is used in the actuarial valuation to determine the cost of benefits accruing for employers who continue to admit new members. This means that the future service contribution rate

is derived as the cost of benefits accruing to employee members over the year following the valuation date expressed as a percentage of members' pensionable pay over that period. The future service rate will be stable if the profile of the membership (age, gender etc) is stable.

For employers who no longer admit new members, the Attained Age valuation method is normally used. This means that the contribution rate is derived as the average cost of benefits accruing to members over the period until they die, leave the Fund or retire. This approach should lead to more stable employer contribution rates than adoption of the Projected Unit method for closed employers.

Funding Targets and assumptions regarding future investment strategy

For Scheduled Bodies and Admission Bodies with a subsumption commitment from a long-term Scheme Employer of sound covenant, the Administering Authority assumes indefinite investment in a broad range of assets of higher risk than risk free assets.

For Admission Bodies and other bodies whose liabilities are expected to be orphaned on cessation, the Administering Authority will have regard to

- the potential for participation to cease (or for the body to have no contributing members), including whether or not it admits new members, or has set up a subsidiary company to employ staff who do not participate in the Fund,
- the type of service being provided by the employer (eg statutory or not), and the covenant of the employer,
- the potential timing of exit from the Fund,
- the funding target adopted at the previous valuation,
- any likely change in notional or actual investment strategy as regards the assets held in respect of the body's liabilities at the date of cessation (i.e. informed by whether the liabilities will become 'orphaned' or a guarantor exists to subsume the notional assets and liabilities).

The default funding target for Admission Bodies which are not expected to participate in the Fund indefinitely and which would leave orphan liabilities on exit (including where any guarantor may have exited the Fund before the admission body it guarantees), is the "ongoing orphan" funding target. This takes account of the fact that on exit the liabilities will be valued by reference to gilt yields.

For Admission Bodies open to new entrants which are considered to be of sufficiently strong covenant, the Administering Authority may, at its sole discretion, instruct the Actuary to adopt a discount rate above that adopted for ongoing orphan funding target (but below that adopted for the long-term secure scheduled bodies). This is known as the intermediate funding target.

For deferred employers where a DDA is in place the funding target will take into account any likely change in the notional or actual investment strategy as regards the assets held in respect of the body's liabilities at the date the DDA is expected to end and any other factors considered to be relevant by the Administering Authority on the advice of the Actuary, which may include, without limitation:

- the agreed period of the DDA;
- the type/group of the employer;
- the business plans of the employer;
- an assessment of the financial covenant of the employer;
- any contingent security available to the Fund or offered by the employer such as a guarantor or bond arrangements, charge over assets, etc.

The Fund is deemed to be fully funded when the assets are equal to or greater than 100% of the Funding Target, where the funding target is assessed based on the sum of the appropriate funding targets across all the employers/groups of employers.

Other Aspects of Funding Strategy

Recovery Periods

Where a valuation reveals that the Fund is in surplus or deficiency against the Funding Target, employer contribution rates will be adjusted to target restoration of full funding over a period of years (the Recovery Period). The Recovery Period applicable for each participating employer is set by the Fund Actuary in consultation with the Administering Authority and the employer, with a view to balancing the various funding requirements against the risks involved due to such issues as the financial strength of the employer and the nature of its participation in the Fund.

The Administering Authority recognises that a large proportion of the Fund's liabilities are expected to arise as benefit payments over long periods of time. For employers of sound covenant, and in the context of the LGPS as a statutory scheme, the Administering Authority is prepared

to agree to Recovery Periods which are longer than the average future working lifetime of the membership of that employer. The Administering Authority recognises that when employers have a deficit in the Fund such an approach is consistent with the aim of keeping employer contribution rates as nearly constant as possible. However, the Administering Authority also recognises the risk in relying on long recovery periods and has agreed with the Fund Actuary a limit of 22 years for employers in surplus and 19 years for employers in deficit. The Administering Authority's policy is to agree Recovery Periods which strike an appropriate balance between risk; affordability and stability of contributions within this framework.

For deferred employers (where there are no active members), it is expected that the maximum recovery period will be the remaining period of the DDA.

Grouping

In some circumstances it may be desirable to group employers within the Fund together for funding purposes (ie to calculate employer contribution rates). Reasons might include reduction of volatility of contribution rates for small employers, facilitating situations where employers have a common source of funding or accommodating employers who wish to share the risks related to their participation in the Fund.

The Administering Authority recognises that grouping can give rise to cross subsidies from one employer to another over time. The Administering Authority's policy is to review the position at each valuation to check if the rationale for grouping continues to apply. If not employers will have their own contribution rates. For employers with more than 50 contributing members, the Administering Authority would look for evidence of homogeneity between employers before considering grouping. For employers whose participation is for a fixed period grouping is unlikely to be permitted.

All employers in the Fund are grouped together in respect of the risks associated with payment of benefits on death in service and tier 1 and 2 ill-health benefits – in other words, the cost of such benefits is shared across the employers in the Fund. These benefits can cause funding strains which could be significant for some of the smaller employers without insurance or sharing of risks. The Fund, in view of its size, does not see it as cost effective or necessary to insure these benefits externally and this is seen as a pragmatic and low cost approach to spreading the risk.

Currently there is one group of employers in the Fund pooled together for funding and contribution purposes. This group is funded on the same funding target as the main scheduled bodies. All risks are shared within this group apart from the payment of deficit contributions.

Where employers are grouped together entirely for funding purposes, this will only occur with the consent of the employers involved.

Stepping

Again, consistent with the aim to keep employer contributions as nearly constant as possible, the Administering Authority will consider, at each valuation, whether new contributions should be payable immediately, or should be reached by a series of steps over future years. The Administering Authority will discuss with the Fund Actuary the risks inherent in such an approach, and will examine the financial impact and risks associated with each employer.

Where employer contribution changes are being stepped in, the Administering Authority's policy is that in the normal course of events no more than six equal annual steps will be permitted (and ideally no more than three steps when contributions are being increased). Where stepped increases are agreed, the Administering Authority will ensure that the employer recognises that this is a mechanism by which contributions can be smoothed and that it represents a deferral of costs rather than a reduction, i.e. by paying less in the short term higher contributions are likely to be required in the longer-term.

Where the expected remaining time until the employer exits the Fund is such that a shorter period is appropriate, or in other exceptional circumstances, a shorter stepping period with a bespoke stepping pattern may be permitted.

Long term cost efficiency

In order to ensure that measures taken to maintain stability of employer contributions are not inconsistent with the statutory objective for employer contributions to be set so as to ensure the long-term cost efficiency of the Fund, the Administering Authority has assessed the actual contributions payable by considering:

- The implied average deficit recovery period, allowing for the stepping of employer contribution changes;
- The investment return required to achieve full funding over the recovery period; and

- How the investment return compares to the Administering Authority's view of the expected future return being targeted by the Fund's investment strategy.
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Inter-valuation funding calculations

In order to monitor developments and as part of its overall risk management strategy, the Administering Authority may from time to time request informal valuations or other calculations. Further details of the Administering Authority's policy in relation to:

- reviewing contributions for employers expected to exit under Regulation 64(4); and
- otherwise reviewing employer contributions between valuations as permitted by Regulation 64A

are set out in Sections 5 and 6 respectively.

Notional Sub-Funds for individual employers

Notional sub-funds

In order to establish contribution rates for individual employers or groups of employers it is convenient to notionally subdivide the Fund as a whole between the employers (or group of employers where grouping operates), as if each employer had its own notional sub-fund within the Fund.

This subdivision is for funding purposes only. It is purely notional in nature and does not imply any formal subdivision of assets, nor ownership of any particular assets or groups of assets by any individual employer or group. The sub-Fund notionally allocated for the purpose of determining ongoing contributions may differ to that allocated at exit.

Roll-forward of sub-funds

The notional sub-fund allocated to each employer's or group's liabilities for determining ongoing contributions during its period of participation in the Fund will be rolled forward allowing for all cashflows associated with that employer's or group's membership, including contribution income, benefit outgo, transfers in and out and investment income allocated as set out below. In general no allowance is made for the timing of contributions and cashflows for each year are assumed to be made half way through the year with investment returns assumed to be uniformly earned over that year. However, where significant one-off employer related cashflows have been received or paid, allowance is made for the timing of such contributions.

Further adjustments are made for:

- A notional deduction to meet the expenses paid from the Fund in line with the assumption used at the previous valuation.
- Allowance for death in service lump sum benefits shared across all employers in the Fund (see above)
- Allowance for any known material internal transfers in the Fund (cashflows will not exist for these transfers). The Fund Actuary will assume an estimated cashflow equal to the value of the liabilities determined using non club cash equivalent transfer value factors transferred from one employer to the other unless some other approach has been agreed between the two employers.
- An overall adjustment to ensure the notional assets attributed to each employer is equal to the total assets of the Fund which will take into account any gains or losses related to the orphan liabilities.

In some cases information available will be incomplete and in such circumstances and where, in the opinion of the Fund Actuary, the cashflow data which is unavailable is of low materiality, estimated cashflows will be used.

There may be circumstances where the results from the above approach requires further adjustment, for example (but not limited to) where changes in legislation are deemed by the Administering Authority to require further adjustments to notional sub-funds (likely to be where legislation has a retrospective effect and means the initial asset allocation when an employer joined the Fund needs to be revisited), or where other new information has become available that is material to the calculation of a notional sub fund (e.g. revised member data or changes in market conditions).

Attribution of investment income

Where the Administering Authority has agreed with an employer that it will have a tailored asset portfolio assumed to be allocated to its notional sub-fund, the assets notionally allocated to that sub-fund will be credited with a rate of return appropriate to the agreed notional asset portfolio.

Where the employer has not been allocated a tailored notional portfolio of assets, the assets notionally allocated to that employer will be credited with the rate of return earned by the Fund assets as a whole, adjusted for any return credited to those employers for whom a tailored notional asset portfolio exists.



SECTION 5

Special Circumstances related to Employers

Interim reviews for employers

Regulation 64(4) of the Regulations provides the Administering Authority with a power to carry out valuations in respect of employers where there are circumstances which make it likely that an employer will become an exiting employer, and for the Actuary to certify revised contribution rates, between triennial valuation dates.

The Administering Authority's overriding objective at all times in relation to participating employers is that, where possible, there is clarity over the Funding Target for that body, and that contribution rates payable are appropriate for that Funding Target. However, this is not always possible as any date of exit may be unknown (for example, participation may be assumed at present to be indefinite), and also because market conditions change daily.

The Administering Authority's general approach in this area is as follows:

- Where the date of exit is known, and is more than 3 years hence, or is unknown and assumed to be indefinite, interim valuations will generally not be carried out at the behest of the Administering Authority.
- For Transferee and Schedule 2 Part 3 (1)(d) Admission Bodies falling into the above category, the Administering Authority sees it as the responsibility of the relevant Scheme Employer to instruct it if an interim valuation is required. Such an exercise would be at the expense of the relevant Scheme Employer unless otherwise agreed.
- A material change in circumstances, such as the date of exit becoming known, material membership movements or material financial information coming to light may cause the Administering Authority to informally review the situation and subsequently formally request an interim valuation.
- For admissions due to cease within the next 3 years, the Administering Authority will keep an eye on developments and may see fit to request an interim valuation at any time.

Notwithstanding the above guidelines, the Administering Authority reserves the right to request an interim valuation

of any employer at any time in accordance with Regulation 64(4).

Regulation 64A of the Regulations provides the Administering Authority with a power to obtain a revision of the rates and adjustments certificate in certain other circumstances. Further details of the Administering Authority's policy in relation to Regulation 64A are set out in Section 6.

Guarantors

Some Admission Bodies may participate in the Fund by virtue of the existence of a Guarantor. The Administering Authority maintains a list of employers and their associated Guarantors and monitors the exposure of the guarantors. The Administering Authority, unless notified otherwise, sees the duty of a Guarantor to include the following:

- If an Admission Body ceases and defaults on any of its financial obligations to the Fund, the Guarantor is expected to provide finance to the Fund such that the Fund receives the amount certified by the Fund Actuary as due, including any interest payable thereon.
- If the Guarantor is an employer in the Fund and is judged to be of suitable covenant by the Administering Authority, the Guarantor may defray some of the financial liability by subsuming the residual liabilities into its own pool of Fund liabilities. In other words, it agrees to be a source of future funding in respect of those liabilities should future deficiencies emerge.
- During the period of participation of the Admission Body a Guarantor can at any time agree to the future subsumption of any residual liabilities of an Admission Body. The effect of that action would generally be to reduce the Funding Target for the Admission Body, which would probably lead to reduced contribution requirements, although in determining the contributions the Administering Authority would have regard to the intentions of the Guarantor and its agreement with the Admission Body. The Guarantor should ensure that it is clear what would happen to any surplus arising on the subsequent exit of the Admission Body, in particular whether or not an exit credit would become payable.

Bonds and other securitization

Schedule 2 Part 3 of the Regulations creates a requirement for a new admission body to carry out, to the satisfaction of the Administering Authority (and Scheme Employer in case of an Admission Body admitted under Schedule 2 Part 3 paragraph (1)(d) of the Regulations), an

assessment taking account of actuarial advice, of the level of risk arising on premature termination of the provision of service or assets by reason of insolvency, winding up or liquidation of the admission body.

Where the level of risk identified by the assessment is such as to require it, the Admission Body shall enter into an indemnity or bond with an appropriate party.

Where, for any reason it is not desirable for an Admission Body to enter into an indemnity bond, the Admission Body is required to secure a guarantee in a form satisfactory to the Administering Authority as set out in Schedule 2 Part 3 paragraph (8).

The Administering Authority's approach in this area is as follows:

- a) In the case of Transferee Admission Bodies and Admission Bodies admitted under Schedule 2 Part 3 (1)(d) of the Regulations and other Admission Bodies where a Scheme Employer acts as guarantor, and so long as the Administering Authority judges the relevant Scheme Employer to be of sufficiently sound covenant, any bond exists purely to protect the relevant Scheme Employer or Guarantor on default of the Admission Body. As such, the Administering Authority's policy is that the relevant Scheme Employer or Guarantor should decide the level of required bond (to the satisfaction of the Administering Authority). The Administering Authority will be pleased to supply some standard calculations provided by the Fund Actuary to aid the relevant Scheme Employer which would satisfy the Administering Authority, but this should not be construed as advice to the relevant Scheme Employer on this matter. The Administering Authority notes that levels of required bond cover can fluctuate and recommends that relevant Scheme Employers review the required cover regularly, at least once a year.
- b) In the case of Admission Bodies as described in a) above, where the Administering Authority does not judge the relevant Scheme Employer to be of sufficiently strong covenant, the Administering Authority will set a level of bond to protect the Fund. The admission will only be able to proceed once the Administering Authority has agreed that is satisfied with the level of bond cover. The Administering Authority notes that levels of required bond cover can fluctuate and will require the relevant Scheme Employer to jointly

review the required cover with it regularly, at least once a year.

- c) For all other Admission Bodies, the Administering Authority will set the required level of bond to protect the Fund. The admission will only be able to proceed once the Administering Authority has agreed the level of bond cover. The Administering Authority notes that levels of required bond cover can fluctuate and will review the required cover regularly, at least once a year.

Subsumed liabilities

Where an employer is ceasing participation in the Fund, it is possible that another employer in the Fund agrees to provide a source of future funding in respect of any emerging deficiencies in respect of those liabilities.

In such circumstances the liabilities are known as subsumed liabilities (in that responsibility for them is subsumed by the accepting employer). For such liabilities the Administering Authority will assume that the investments held in respect of those liabilities will be the same as those held for the rest of the liabilities of the accepting employer. Generally this will mean assuming continued investment in a mix of growth and matching assets.

Orphan liabilities

Where an employer is ceasing participation in the Fund such that it will no longer have any contributing members, unless any residual liabilities are to become subsumed liabilities or a DDA is entered into, the Administering Authority will act on the basis that it will have no further access for funding from that employer once any cessation valuation, carried out in accordance with Regulation 64, has been completed and any sums due have been paid. Residual liabilities of employers from whom no further funding can be obtained are known as orphan liabilities.

The Administering Authority will seek to minimise the risk to other employers in the Fund that any deficiency arises on the orphan liabilities such that this creates a cost for those other employers to make good the deficiency. To give effect to this, the Administering Authority will seek funding from the outgoing employer sufficient to enable it to match the liabilities with low risk investments, generally Government fixed interest and index linked bonds.

To the extent that the Administering Authority decides not to match these liabilities with Government bonds of appropriate term then any excess or deficient returns will

be added to or deducted from the investment return to be attributed to the employer's notional sub-fund.

Liabilities in the Fund which are already orphaned will be assumed to be 100% funded on the appropriate funding target at each triennial valuation. This will be achieved by the Actuary notionally re-allocating assets within the Fund as required.

Exit of employers

Where an employer exits the Fund, an exit valuation will be carried out in accordance with Regulation 64. That valuation will take account of any activity as a consequence of cessation of participation regarding any existing contributing members (for example any bulk transfer payments due) and the status of any liabilities that will remain in the Fund.

The approach adopted to value the departing employer's liabilities for the exit valuation will depend upon the circumstances. In particular, the exit valuation will distinguish between residual liabilities which will become orphan liabilities, and liabilities which will be subsumed by a long-term secure employer such as one of the councils.

In determining the assets notionally allocated to the exiting employer at exit, consideration will be given to the contributions made by the employer to the overall Fund assets during its period of participation in the Fund. Where appropriate, the notional asset value may be subject to a cap of the value of the employer's liabilities at exit calculated using the relevant Funding Target (see below) plus the accumulated value of primary and secondary contributions paid by that employer. In determining the accumulated value of these contributions investment returns will be allocated based on the asset portfolio appropriate to the employer.

Orphan liabilities

For orphan liabilities the Funding Target in the exit valuation of the liabilities will anticipate investment in low risk investments such as Government bonds. This is to protect the other employers in the Fund, as upon exit, the employer's liabilities will become "orphan" liabilities within the Fund, and there is no recourse to that (former) employer if a shortfall emerges in relation to these liabilities after the exit date.

Any deficit or surplus in the Fund in respect of the employer will generally be due to the Fund as a termination contribution, or payable by the Fund to the employer as an exit credit respectively, where the exit date is on or after 14 May 2018.

Subsumed liabilities

For subsumed liabilities the exit valuation of the liabilities will be determined on the basis that the scheme employer providing the subsumption commitment will subsume all assets and liabilities from the exiting employer. No exit credit will be paid to, or any exit debt required from, the exiting employer, unless the exiting employer is in surplus when liabilities are calculated using a Funding Target that anticipates investment in low risk investments such as Government bonds. The assets and liabilities will be subsumed within those of the employer providing the subsumption commitment, with future contribution requirements for this employer being reassessed at each actuarial valuation.

In addition, under either scenario, the Administering Authority may, at its discretion, include additional margins for prudence compared to the approach used for determining ongoing contributions, for example (but not limited to) in relation to regulatory uncertainty (which at the date of this Statement includes uncertainty associated with the McCloud case, the Goodwin case, the cost management process and equalisation of GMP) – see Section 9 on Risks and Countermeasures.

Further, where regulatory changes have been made that impact on the value of accrued benefits but were not reflected in the latest valuation used for determining ongoing contributions, these changes will be allowed for in the exit valuation.

Spreading of exit payments

Where an exit payment is due, unless a DDA is entered into, the Administering Authority's policy is to require a one-off lump sum payment equal to the exit deficit. However, in certain circumstances employers may be able to request spreading of an exit payment on affordability grounds. The Administering Authority's policy on the spreading of exit payments as permitted by Regulation 64B is set out in Section 7.

Deferred Debt Agreements

Where an employer ceases to have any active members or would otherwise become an exiting employer, it may request that the Administering Authority enters into a Deferred Debt Agreement (DDA) as permitted by Regulation 64(7A) and become a deferred employer.

The Administering Authority's policy in relation to use of Regulation 64(7A) is set out in Section 8.

SECTION 6

Reviewing employer contributions between valuations under Regulation 64A

Background

This section sets out the Administering Authority's policies and procedures in relation to any amendment of employer contributions between formal valuations as permitted by Regulation 64A.

The Administering Authority will consider reviewing employer contributions between formal valuations in the following circumstances:

- it appears likely to the Administering Authority that the amount of the liabilities arising or likely to arise has changed significantly since the last valuation;
- it appears likely to the Administering Authority that there has been a significant change in the ability of the Scheme employer or employers to meet the obligations of employers in the Scheme; or
- Scheme employer or employers have requested a review of Scheme employer contributions and have undertaken to meet the costs of that review

For the avoidance of doubt, the Administering Authority will not consider a review of contributions purely on the grounds of a change in market conditions affecting the value of assets and/or liabilities.

Factors considered

In determining whether or not a review should take place, the Administering Authority will consider the following factors (noting that this is not an exhaustive list):

- the circumstances leading to the change in liabilities arising or likely to arise, for example whether this is the result of a decision by the employer, such as the restructuring of an employer, a significant outsourcing or transfer of staff, closure to new entrants, material redundancies or significant pay awards, or other factors such as ill-health retirements, voluntary withdrawals or the loss of a significant contract.
- the materiality of any change in the employer's membership or liabilities, taking account of the Actuary's view of how this might affect its funding position, primary or secondary contribution rate.
- whether, having taken advice from the Actuary, the Administering Authority believes a change in ongoing

funding target or deficit recovery period would be justified, e.g. on provision or removal of any security, subsumption commitment, bond, guarantee, or other form of indemnity in relation to the employer's liabilities in the Fund.

- the materiality of any change in the employer's financial strength or longer-term financial outlook, based on information supplied by the employer and supported by a financial risk assessment or more detailed covenant review carried out by the Fund Actuary or other covenant adviser to the Fund.
- the general level of engagement from the employer and its adherence to its legal obligations as set out in the Pensions Administration Strategy Statement and elsewhere, including the nature and frequency of any breaches such as failure to pay contributions on time and data quality issues due to failure to provide new starter or leaver forms.

Risk assessment

In determining whether or not a review should take place, the Administering Authority will generally focus on the materiality of any potential changes in the context of the employer concerned; its financial position and current contribution levels. As a matter of principle, the Administering Authority does not consider that a review is not justified just because an employer is small in the context of the Fund as a whole, noting that failure to act could make discussions at the next formal valuation more difficult and compound the risk to the Fund. However, in determining the extent and speed of any changes to the employer's contributions the Administering Authority will consider the effect on the overall funding position of the Fund, i.e. other Fund employers.

Where contributions are being reviewed for an employer with links to another Fund employer, particularly where this is a formal organisational or contractual link, e.g. there is a tripartite admission agreement, an ownership relationship or a formal guarantee or subsumption commitment is in place, the Administering Authority will consider the potential risk/impact of the contribution review on those other employer(s), taking advice from the Fund Actuary as required.

Consultation

It is expected that in most cases the employer will be aware of the proposed review of their contributions since this will be triggered by an employer's action and employers should be aware of the need to engage with the Administering Authority in relation to any activity which could materially affect their liabilities or ability to meet those liabilities. The requirements on employers to inform the Administering Authority of certain events are set out in the Pensions Administration Strategy.

In other cases information will be required from the employer, e.g. in relation to its financial position and business plans which could be the catalyst for informing the employer that a review is being proposed. In all cases the Administering Authority will advise the employer that a review is being carried out and share the results of the review and any risk or covenant assessment as appropriate. It should be noted that the fact of a review being carried out does not automatically mean that contributions will be amended (up or down) since that will depend upon the materiality of the changes and other factors such as the outcome of discussions with the employer and any related/linked employer in the Fund and the proximity to the next formal valuation.

Where, following representations from the employer, the Administering Authority is considering not increasing the employer's contributions following a review, despite there being good reason to do so from a funding and actuarial perspective, e.g. if it would precipitate the failure of the employer or otherwise seriously impair the employer's ability to deliver its organisational objectives or it is expected that the employer's financial position will improve significantly in the near-term, the Administering Authority will consult with any related/linked employers (including any guarantor or employer providing a subsumption commitment) and, where appropriate, the largest employers in the Fund with a view to seeking their agreement to this approach.

Request process

Before requesting a review, employers should consider the regulatory requirements and the Fund's policy as set out above and satisfy themselves that there has been a relevant change in the expected amount of liabilities or their ability to meet those liabilities. The employer should contact the Pensions Service Manager, Catherine.black@rctcbc.gov.uk and complete the necessary information requirements for submission to the Administering Authority in support of their application.

The Administering Authority will consider the employer's request and may ask for further information or supporting documentation/evidence as required. If the Administering Authority, having taken actuarial advice as required, is of the opinion that a review is justified, it will advise the employer and provide an indicative cost. Employers should be aware that all advisory fees incurred by the Fund associated with a contribution review request, whether or not this results in contributions being amended, will be recharged to the employer.

Other considerations

The Administering Authority will carry out an annual assessment of the risk for Tier 3 employers and any others as considered appropriate. This will help identify whether a contribution review is required and is expected to be carried out as at each 30 September with any contribution changes effective from the following 1 April.

More generally, the Administering Authority may carry out a review at any time during the valuation cycle where it becomes aware that a review is required. In such cases the employer will be expected to provide the requested information within one month of request and the review will be completed within 6 weeks of the provision of all requested information, or completion of the risk/covenant assessment if later.

The Administering Authority will consult with the employer on the timing of any contribution changes and there will be a minimum of 4 weeks' notice given of any contribution increases. In determining whether, and when, any contribution changes are to take effect the Administering Authority will also take into account the timing of contribution changes flowing from the next formal valuation. As a result, contribution reviews are unlikely to be carried out during the 12 month period from the valuation date although if there were any material changes to the expected amount of liabilities arising or the ability of the employer to meet those liabilities during that period, this should be taken into account when finalising the Rates and Adjustments Certificate flowing from the valuation.

Appeals process

Any Employer appeal against the Administering Authority's determination must be made in writing to the Service Director, Pensions, Procurement & Transactional Services within 6 months of being notified of the determination.

An appeal will require the Employer to evidence one of the following:

- deviation from the published policy or process by the Administering Authority, or
 - any further information (or interpretation of information provided) which could influence the outcome, noting new evidence will be considered at the discretion of the Administering Authority.
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SECTION 7

Spreading of exit payments under Regulation 64B

Spreading of exit payments

Where an exit payment is due, unless a DDA is entered into, the Administering Authority's policy is to require a one-off lump sum payment equal to the exit deficit. However, in certain circumstances employers may be able to request spreading of an exit payment on affordability grounds. The Administering Authority's policy on the spreading of exit payments as permitted by Regulation 64B is set out below:

It is envisaged that spreading of exit payments will only be considered at the request of an employer. The Administering Authority will then engage/consult with the employer to consider its application and determine whether or not spreading the exit payment is appropriate and the terms which should apply.

Process and factors considered

In determining whether or not to permit an exit payment to be spread, the Administering Authority will consider factors including, but not limited to:

- the ability of the employer to make a single capital payment;
- whether any security is in place, including a charge over assets, bond, guarantee or other indemnity;
- whether the overall recovery to the Fund is likely to be higher if spreading the exit payment is permitted.

In determining the employer's ability to make a single payment the Administering Authority will seek actuarial, covenant or legal advice as required. Where the Administering Authority considers that the employer is financially able to make a single capital payment it will not normally be appropriate for the exit payment to be spread.

The employer will be required to provide details of its financial position, business plans and financial forecasts and such other information as required by the Administering Authority in order for it to make a decision on whether or not to permit the exit payment to be spread. This information must be provided within 2 months of request.

In determining the appropriate length of time for an exit payment to be spread, the Administering Authority will consider the affordability of the instalments using different spreading periods for the employer. The default spreading period will be three years but longer periods of up to ten years will be considered where the Administering Authority is

satisfied that this doesn't pose undue risk to the Fund in relation to the employer's ability to continue to make payments over the period.

Whilst the Administering Authority's preference would be for an employer to request spreading of any exit payment in advance of the exit date, it is acknowledged that a final decision by the employer (and the Administering Authority) on whether this will be financially beneficial/appropriate may not be possible until the employer has exited. Exiting employers will be advised of the exit deficit and the spreading of any payment will only be considered at the request of the employer. Where there is a guarantor, the guarantor will also be consulted and any agreement to spread the exit deficit may be conditional on the guarantee continuing in force during the spreading period.

The amount of the instalments due under an exit deficit spreading agreement will generally be calculated as level annual amounts allowing for interest over the spreading period in line with the discount rate used to calculate the exit liabilities. Where the exit amount is significant, monthly payments may be required or the Administering Authority may require a higher initial payment with lower annual payments thereafter to reduce the risk to the Fund. Alternative payment arrangements may be made in exceptional circumstances as long as the Administering Authority is satisfied that they do not materially increase the risk to the Fund.

Agreement, costs and review

Where it has been agreed to spread an exit payment the Administering Authority will advise the employer in writing of the arrangement, including the spreading period; the annual payments due; interest rates applicable; other costs payable* and the responsibilities of the employer during the spreading period. Where a request to spread an exit payment has been denied the Administering Authority will advise the employer in writing and provide a brief explanation of the rationale for the decision.

*Employers will be asked to pay all advisory costs associated with the spreading agreement as well as calculation of the exit deficit (these costs will not be spread).

The Administering Authority will generally review spreading agreements as part of its preparation for each triennial valuation and will take actuarial, covenant, legal and other advice as considered necessary. In addition, employers will be expected to engage with the Administering Authority during the spreading period and adhere to the notifiable events framework as set out in the Pensions Administration

Strategy. If the Administering Authority has reason to believe the employer's circumstances have changed such that a review of the spreading period (and hence the payment amounts) is appropriate, it will consult with the employer and a revised payment schedule may be implemented. Whilst this review may also consider the frequency of payments, it should be noted that it is not envisaged that any review will consider changes to the original exit amount nor interest rate applicable. An employer will be able to discharge its obligations under the spreading arrangement by paying off all future instalments at its discretion. The Administering Authority will seek actuarial advice in relation to whether or not there should be a discount for early payment given interest will have been added in line with the discount rate used for the exit valuation.

SECTION 8

Deferred Debt Agreements under Regulation 64(7A)

Deferred Debt Agreements

Where an employer ceases to have any active members or would otherwise become an exiting employer, it may request that the Administering Authority enters into a Deferred Debt Agreement (DDA) as permitted by Regulation 64(7A) and become a deferred employer.

The Administering Authority's policy in relation to use of Regulation 64(7A) is set out below.

Factors considered

In determining whether or not to enter into a DDA with an employer the Administering Authority will take into account the following factors, including but not limited to:

- the materiality of the employer and any exit deficit in terms of the Fund as a whole;
- the risk to the Fund of entering into a DDA, in terms of the likelihood of the employer failing before the DDA has ended, based on information supplied by the employer and supported by a financial risk assessment or more detailed covenant review carried out by the Fund Actuary or other covenant adviser
- the rationale for the employer requesting a DDA, particularly if the Administering Authority believes the employer would be able to make an immediate payment to cover the exit deficit; and
- whether an up front payment will be made towards the deficit, and/or any security is, or can be, put in place, including a charge over assets, bond, guarantee or other indemnity, to reduce the risk to other employers.

Where it is expected that the employer's covenant may materially weaken over time the Administering Authority is very unlikely to consider entering into a DDA with that employer. Further, where an employer can demonstrably meet the exit payment in a single instalment, the Administering Authority would be unlikely to enter into a DDA unless it was clear that this wouldn't increase risk to the Fund, e.g. if the employer was fully taxpayer-backed and sufficient assurance was in place that all contributions due, including any residual deficit at the end of the DDA, would be met in full.

Process, agreement, costs and review

It is envisaged that DDAs will only be entered into at the request of an employer. In all cases, the Administering Authority will engage/consult with the employer to determine whether or not a DDA is appropriate and the terms which should apply. As part of its application for a DDA, the Administering Authority will require information from the employer to enable the Administering Authority to take a view on the employer's strength of covenant. Information will also be required on an ongoing basis to enable the employer's financial strength/covenant to be monitored. It is expected that DDAs will be monitored on an annual basis unless circumstances dictate otherwise. Monitoring may be more frequent as the end of the period of the DDA approaches.

Employers should be aware that all advisory fees incurred by the Fund associated with a request for a DDA, whether or not this results in an agreement being entered into, and its ongoing monitoring, will be recharged to the employer.

The Administering Authority will provide a standard form of agreement for DDAs, which it will require employers (and any guarantors) to sign up to. The matters which the Administering Authority will reflect in the DDA, include:

- an undertaking by the employer to meet all requirements on Scheme employers, including payment of the secondary rate of contributions, but excluding the requirement to pay the primary rate of contributions;
- a provision for the DDA to remain in force for a specified period, which may be varied by agreement of the Administering Authority and the deferred employer as long as the total period does not exceed 10 years;
- a provision that the DDA will terminate on the first date on which one of the following events occurs:
 - (a) the deferred employer enrolls new active members;
 - (b) the period specified, or as varied, elapses;
 - (c) the take-over, amalgamation, insolvency, winding up or liquidation of the deferred employer;
 - (d) the Administering Authority serves a notice on the deferred employer that it is reasonably satisfied that the deferred employer's ability to meet the contributions payable under the deferred debt arrangement has weakened materially or is likely to weaken materially in the next 12 months; or
 - (e) the Fund Actuary assesses that the deferred employer has paid sufficient secondary contributions to cover the exit

payment that would have been due if the employer had become an exiting employer on the calculation date.

- the responsibilities of the deferred employer
- the circumstances triggering a cessation of the arrangement leading to an exit payment (or credit) becoming payable, in addition to those set out in Regulation 64 (7E) and above

It is expected that the consultation process with the employer will include discussions on the precise details of the DDA, although the purpose of providing a standard form of agreement is to make the process easier, and quicker and therefore it is not envisaged that there will be material changes to the standard.

The Administering Authority will monitor the funding position and risk/covenant associated with deferred employers on a regular basis. This will be at least triennially and most likely annually, but the frequency will depend on factors such as the size of the employer and any deficit and the materiality of movements in market conditions or the employer's membership.

The circumstances in which the Administering Authority may consider seeking to agree a variation to the length of the agreement under regulation 64(7D) include:

- where the exit deficit has reduced (increased) such that it is reasonable to reduce (extend) the length of the recovery period and associated period of the DDA assuming that, in the case of the latter, this does not materially increase the risk to the other employers/Fund
- where the deferred employer's business plans, staffing levels, finances or projected finances have changed significantly, but, in the case of a deterioration, the Administering Authority, having taken legal, actuarial, covenant or other advice as appropriate, does not consider that there is sufficient evidence that deferred employer's ability to meet the contributions payable under the DDA has weakened materially, or is likely to weaken materially in the next 12 months
- where the level of security available to the Fund has changed in relation to the DDA, as determined by the Administering Authority, taking legal, actuarial or other advice as appropriate

At each triennial valuation, or more frequently as required, the Administering Authority will carry out an analysis of the financial risk or covenant of the deferred employer, considering actuarial, covenant, legal and other advice as

necessary. Where supported by the analysis and considered necessary to protect the interests of all employers, the Administering Authority will serve notice on the deferred employer that the DDA will terminate on the grounds that it is reasonably satisfied that the deferred employer's ability to meet the contributions payable under the deferred debt arrangement has weakened materially, or is likely to weaken materially in the next 12 months, as set out under regulation 64(7E)(d).

Employers should be aware that all advisory fees incurred by the Fund associated with consideration of a DDA for an exiting employer, whether or not this results in a DDA being entered into, will be recharged to the employer. This will include actuarial, legal, covenant and other advice and the costs of monitoring the arrangement as well as the initial set up. Estimated costs can be provided on request. All fees must be paid up front and cannot be added to any secondary contributions payable under the DDA.

It is expected that employers will make a request to consider a DDA before they would otherwise have exited the Fund under Regulation 64(1) and that a DDA should be entered into within 3 months of that date. The employer should continue to make secondary contributions at the prevailing rate whilst the DDA is being considered unless the Administering Authority, having taken actuarial and other advice as appropriate, determines that increased contributions should be payable. In exceptional circumstances, e.g. where there has been a justifiable delay due to circumstances outside of the employer's control, and at the sole discretion of the Administering Authority, a DDA may be entered into more than 3 months after the exit date.

Deferred employers will be expected to engage with the Administering Authority during the period of the DDA and adhere to the notifiable events framework as set out in the Pensions Administration Strategy as well as providing financial and other information on a regular basis. This will be necessary to support the effective monitoring of the arrangement and will be a requirement of the DDA.

SECTION 9

Identification of risks and counter measures

Approach

The Administering Authority seeks to identify all risks to the Fund and to consider the position both in aggregate and at an individual risk level. Those risks most likely to impact on the funding strategy are investment risk, liability risk, liquidity/maturity risk, regulatory/compliance risk, employer risk and governance risk.

The Administering Authority will monitor the risks to the Fund, and will take appropriate action to limit the impact of these both before, and after, they emerge wherever possible. The Administering Authority will ensure that funding risks are included within their overarching risk management framework and strategy, linking to their risk register and risk management policy as appropriate and includes defining a role for the Local Pension Board within this framework.

Investment Risk

This covers items such as the performance of financial markets and the Fund's investment managers, asset reallocation in volatile markets, leading to the risk of investments not performing (income) or increasing in value (growth) as forecast. Examples of specific risks would be:

- assets not delivering the required return (for whatever reason, including manager underperformance)
- systemic risk with the possibility of interlinked and simultaneous financial market volatility
- insufficient funds to meet liabilities as they fall due
- inadequate, inappropriate or incomplete investment and actuarial advice is taken and acted upon
- counterparty failure

The specific risks associated with assets and asset classes are:

- equities – industry, country, size and stock risks
- fixed income - yield curve, credit risks, duration risks and market risks
- alternative assets – liquidity risks, property risk, alpha risk
- money market – credit risk and liquidity risk
- currency risk
- macroeconomic risks
- environmental; social and corporate governance risks

The Fund mitigates these risks through diversification, permitting investment in a wide variety of markets and

assets, and through the use of specialist managers with differing mandates in addition to the internal investment management team, which has a wide variety of experience within its members.

The performance of both markets and managers is reviewed regularly by the Investment Advisory Panel, which has the appropriate skills and training required to undertake this task.

Climate change

The systemic risks posed by climate change and the policies implemented to tackle them will fundamentally change economic, political and social systems and the global financial system. They will impact every asset class, sector, industry and market in varying ways and at different times, creating both risks and opportunities for investors. The Administering Authority and Investment Advisory Panel keeps the effect of climate change on future returns under review and will commission modelling or advice from the Fund Actuary on the potential effect on funding as required.

Liability risk

The main risks include discount rates, pay and price inflation, changing retirement patterns, mortality and other demographic risks. Some of these risks will affect the amount of benefit payments; others will affect the value of benefit payments, i.e. level of assets deemed to be required to meet those benefit payments (the funding target).

The Administering Authority will ensure that the Fund Actuary investigates demographic, pay and pension increase experience at each valuation and reports on developments. The demographic assumptions are intended to be best estimate, informed by Fund experience and wider evidence where needed, e.g. the mortality assumptions are informed by a postcode analysis carried out by the Fund Actuary's specialist longevity team and the projections model released by the Continuous Mortality Investigation of the Institute and Faculty of Actuaries. If the Administering Authority becomes aware of any material changes in population mortality which may also be reflected in the Fund's experience it will ask the Fund Actuary to report on the effect on the funding position and employer contributions.

The Fund Actuary will also provide quarterly funding updates to assist the Administering Authority in its monitoring of the financial liability risks. The Administering Authority will, as far as practical, monitor changes in the age profile of the Fund membership early retirements,

redundancies and ill health early retirements in the Fund and, if any changes are considered to be material, ask the Fund Actuary to report on their effect on the funding position and employer contributions.

If significant changes in the value of the liability become apparent between valuations, the Administering Authority will notify the affected employers of the anticipated impact on costs that will emerge at the next valuation and consider whether to require the review of the bonds that are in place for Admission Bodies. It will also consider the extent to which such changes can or should be allowed for in exit valuations, taking advice from the Fund Actuary.

Where it appears likely to the Administering Authority that the amount of the liabilities arising or likely to arise has changed significantly since the last valuation the Administering Authority may consider revising an employer's contributions as permitted by Regulation 64A. Details of the Administering Authority's policy in this area are set out in Section 6.

Liquidity and Maturity risk

This is the risk of a reduction in cash flows into the Fund, or an increase in cash flows out of the Fund, or both, which can be linked to changes in the membership and, in particular, a shift in the balance from contributing members to members drawing their pensions. Changes in the funding position and hence (secondary) employer contributions can also affect the cashflow position since it is not always possible to deliver complete stability of contributions. Changes within the public sector and to the LGPS itself may affect the maturity profile of the LGPS and have potential cash flow implications. For example,

- budget cuts and headcount reductions could reduce the active (contributing) membership and increase the number of pensioners through early retirements;
- an increased emphasis on outsourcing and other alternative models for service delivery may result in falling active membership (e.g. where new admissions are closed or scheduled employers establish wholly owned companies which do not fully participate in the LGPS),
- public sector reorganisations may lead to a transfer of responsibility between different public sector bodies, (e.g. to bodies which do not participate in the Fund or the LGPS),
- scheme changes, for example lower member contributions, as provisionally agreed as part of the 2016

Scheme Advisory Board cost management process will lead to lower member contributions which may not be immediately matched by higher employer contributions,

- an increase in the take-up of the 50/50 option (whether on affordability grounds or to avoid tax charges) will reduce member contributions to the Fund

The Administering Authority seeks to maintain regular contact with employers to mitigate against the risk of unexpected or unforeseen changes in maturity or other changes leading to cashflow or liquidity issues. The Administering Authority also commissions the Fund Actuary to provide projections of benefit payments and contributions based at each valuation and monitors the cashflow position on a regular basis.

Regulatory and compliance risk

Regulatory risks to the scheme arise from changes to general and LGPS specific regulations, taxation, national changes to pension requirements, or employment law. There are a number of uncertainties associated with the benefit structure at the time of the latest formal review of this Statement, including:

- How Government will address the issues of GMP equalisation.
- The timing and provisions of any final regulations in response to the McCloud/Sargeant cases which ruled that the transitional protections implemented in the Firefighters' and Judges' Pension Schemes were illegal age discrimination.
- The outcome of the cost management process as at 31 March 2016 and 31 March 2020 and whether the agreement reached in relation to the 2016 Scheme Advisory Board (SAB) process for member contributions to be reduced and benefits enhanced to achieve an additional cost of 0.9% of pay will be implemented.

Details of the allowance made for these uncertainties in the 2019 valuation are set out in Appendix 1.

The Goodwin case in which an Employment Tribunal ruled (in relation to the Teachers' Pension Scheme) that the less favourable provisions for survivor's benefits of a female member in an opposite sex marriage compared to a female in a same sex marriage or civil partnership amounts to direct discrimination on grounds of sexual orientation. Following a written ministerial statement by the chief secretary to the Treasury on 20 July 2020 it is expected that changes will be

made to the LGPS Regulations to reflect the ruling, but no changes have yet been proposed.

Redundancy early retirement provisions - with effect from 4 November 2020 a cap on exit payments made by public sector employers came into effect, including the cost of early payment of LGPS pensions for those over aged 55. These new Regulations have since been revoked but Government is expected to come forward with new proposals and it is not yet clear what the final provisions will be for the LGPS nor whether or how they will apply to employers in Wales.

Consultations which have been published but not yet taken forward by Government include changes relating to Fair Deal arrangements, changes to the valuation cycle although the Administering Authority understands that the 2022 valuation is going ahead as previously planned, and changes to HE/FE sector employers.

The Administering Authority will keep abreast of all the proposed changes. The Administering Authority will normally respond to consultations on these matters where they have an impact on the Fund and ask the Fund Actuary to assess the possible impact on costs of the change. It would encourage employers, who frequently have a greater interest in proposed changes, to respond independently.

Employer risk

These risks arise from the ever-changing mix of employers, from short-term and ceasing employers, and the potential for a shortfall in payments and/or orphaned liabilities where employers are unable to meet their obligations to the Scheme. The response to the COVID-19 pandemic may have adverse consequences in relation to employer finances and their ability to make contributions. The Administering Authority monitors employer payments and expects employers in financial difficulty to engage with the Fund, noting that contributions can be reviewed between formal valuations if the conditions in Regulation 64A and the terms of the Administering Authority's policy, as set out in Section 6, are met.

The Administering Authority maintains a knowledge base on its employers, their basis of participation and their legal status (e.g. charities, companies limited by guarantee, group/subsidiary arrangements) and uses this information to inform the FSS. It has also developed a framework for analysing the risk posed by the most material Tier 3 employers to the Fund which continue to admit new entrants and operates different funding targets to reduce the risk of employers failing and exiting the Fund with a material

shortfall relative to the exit liabilities. It does not consider it appropriate (or affordable for the employers concerned) to eliminate the risk of an unmet exit deficit and will ask the Fund Actuary to review the funding position and level of risk of the short-term and Tier 3 employers between triennial valuations where it believes this is appropriate. In due course it will also ask the Fund Actuary to review the funding position of any deferred employers on a regular basis between triennial valuations, noting that the Regulations specifically provide for a DDA to end when the Actuary assesses that the deferred employer has paid sufficient secondary contributions to cover the exit payment that would have been due if the employer had become an exiting employer on the calculation (review) date.

Governance risk

This covers the risk of unexpected structural changes in the Fund membership (for example the closure of an employer to new entrants or the large scale withdrawal or retirement of groups of staff or establishment of a wholly owned company which does not participate in the Fund, or only partially participates), and the related risk of the Administering Authority not being made aware of such changes in a timely manner.

The Administering Authority's policy is to require regular communication between itself and employers, and to ensure regular reviews of such items as bond arrangements, financial standing of non-tax raising employers and funding levels. Fund will commission triennial reviews of any bonds as part of its risk management. Particular examples are set out below:

Early retirement strain payments

No allowance is made for the additional value of the benefits when a member is made redundant or leaves on the grounds of efficiency. To counter the potential 'strain' (or cost) emerging at the next valuation early retirement strain payments are required from the employer to the Fund to meet this additional cost over a period of no longer than 3 years.

Employers with small and declining number of contributing members

The Administering Authority's view is that employers with no contributing members cannot be charged contributions under Regulation 67 (unless a DDA is entered into). There is a risk of an employer ceasing to pay contributions with a deficit in the Fund, and being unable to pay the exit payment under Regulation 64.

The Administering Authority will monitor employers with declining membership to ensure that funding is close to 100% on the solvency measure by the time the last member leaves service and this may affect the funding strategy accordingly.

Bodies ceasing to exist with unpaid deficiency

Some employers can cease to exist and become insolvent leaving the employers in the Fund open to the risk of an unpaid deficit. For Transferee Admission Bodies and Admission Bodies admitted under Schedule 2 Part 3 (1)(d), any such deficit will be met by the relevant Scheme Employer and there is therefore little risk to other employers in the Fund (provided of course that the relevant Scheme Employer is itself regarded to be of good covenant).

Other employers are more problematic and the Administering Authority will as far as practicable look to reduce risks by use of bond arrangements or ensuring there is a guarantor to back the liabilities of the body.

Recovery period risk

The Administering Authority recognises that permitting surpluses or deficiencies to be eliminated over a Recovery Period rather than immediately introduces a risk that action to restore solvency is insufficient between successive measurements. The Administering Authority will discuss the risks inherent in each situation with the Fund Actuary and to limit the Recovery Period where appropriate. Details of the Administering Authority's policy are set out earlier in this Statement.

Stepping risk

The Administering Authority recognises that permitting contribution rate changes to be introduced by annual steps rather than immediately introduces a risk that action to restore solvency is insufficient in the early years of the process. The Administering Authority will discuss the risks inherent in each situation with the Fund Actuary and limit the number of permitted steps as appropriate. Details of the Administering Authority's policy are set out earlier in this Statement.

APPENDIX 1

Actuarial Valuation as at 31 March 2019

The assumptions and method outlined below reflect the assumptions appropriate to the triennial valuation as at 31 March 2019. They are not appropriate for employer accounting purposes and may be refined for exit valuations as set out in the relevant section of this Statement above. In addition, the financial assumptions will be updated to reflect market conditions appropriate to the date of any future calculations (e.g. for admissions, exits, funding updates and any review of employer contributions before the next valuation due as at 31 March 2022).

Method and assumptions used in calculating the funding target

The actuarial method to be used is the Projected Unit method, under which the salary increases assumed for each member are projected until that member is assumed to leave active service by death, retirement or withdrawal from service.

Principal assumptions

Investment return (discount rate)

The discount rate for the 2019 valuation for employers subject to the Scheduled and Subsumption Body Funding Target is 4.25% p.a. for the periods pre and post retirement, based on a Probability of Funding Success of 75%.

For employers subject to the Ongoing Orphan Body Funding Target the discount rate is 3.85% p.a. in service (equivalent to the in service discount rate for secure scheduled bodies less 0.4% p.a.) and 1.6% p.a. left service (which is equivalent to the yield on long-dated fixed interest gilts at the valuation date plus 0.3% p.a. in light of market expectations of the possible future increases in gilt yields).

For employers subject to the Intermediate Funding Target the discount rate is 3.85% p.a. in service and 3.75% p.a. left service left service.

For liabilities which are already orphaned the discount rate is 1.3% p.a. (equivalent to the yield on long-dated fixed interest gilts at the valuation date).

Inflation (Retail Prices Index (RPI) and Consumer Prices Index (CPI) inflation)

The RPI inflation assumption is taken to be the Capital Market Assumption at the valuation date as produced by Aon Solutions UK Limited. In formulating the Capital Market Assumption, both consensus forecasts and the inflation risk premium are considered.

The CPI inflation assumption at the valuation date is set as RPI inflation less 1.1%.p.a. The deduction has been set having regard to the estimated difference between RPI and CPI arising from the difference in the calculation approach between the two indices. This estimate (and hence the assumed difference between CPI and RPI) will vary from time to time.

Salary increases

The assumption for real salary increases (salary increases in excess of consumer price inflation) will be determined by an allowance of 1.25% p.a. over the consumer price inflation assumption as described above.

Pension increases

Increases to pensions are assumed to be in line with the inflation (CPI) assumption as determined above. This is modified appropriately to reflect any benefits which are not fully indexed in line with the CPI (e.g. Guaranteed Minimum Pensions in respect of service prior to April 1997, other than for those reaching SPA between 6 April 2016 and 5 April 2021).

Mortality

Post-retirement Mortality

Base Rates

Normal Health: Standard SAPS S2 Normal Health – Heavy Amounts tables, year of birth base rates, adjusted by a scaling factor.

Ill-health: Standard SAPS S2 Ill-health tables, year of birth base rates adjusted by a scaling factor.

Scaling Factors

Rates adjusted by scaling factors determined by Fund experience and analysis by post code using the Fund Actuary's proprietary longevity model.

Male actives retiring in normal health	95%
Male deferreds retiring in normal health	90%
Male pensioners retiring in normal health and male dependants	85%
Female actives and deferreds retiring in normal health	100%
Female pensioners retiring in normal health	95%
Female dependants	105%
Contingents of current male actives	110%
Contingents of current male deferreds and pensioners	105%
Contingents of current female actives	100%
Contingents of current female deferreds and pensioners	95%
Male ill health pensioners	115%
Female ill health pensioners	100%

Future improvement to base rates

An allowance for improvements in line with the CMI 2018 with $Sk=7.5$, for men or women as appropriate, with a long term rate of improvement of 1.50% p.a.

Pre-retirement mortality

Males: As for normal health retirements but with a 40% scaling factor

Females: As for normal health retirements but with a 40% scaling factor

Retirements age

Member Group*	Assumed age at retirement
Group 1 and Group 2 members	63
Group 3 members (Ro85 age = 60)	63
Group 3 members (Ro85 age > 60)	65
Group 4 members (Joiners pre 1 April 2014)	65
Group 4 members (Joiners post 31 March 2014)	State Pension Age

* Group 1 to Group 4 members are as defined in the early payment of pension guidance (see <http://lgpslibrary.org/assets/actgui/ew/Early20160418.pdf>)

Withdrawals

Allowance is made for withdrawals from service. On withdrawal, members are assumed to leave a deferred pension in the Fund and are not assumed to exercise their option to take a transfer value.

Retirement due to ill health

Allowance is made for retirements due to ill health. Proportions assumed to fall into the different benefit tiers applicable after 1 April 2008 are:

Tier 1 (upper tier)	80%
Tier 2 (middle tier)	15%
Tier 3 (lower tier)	5%

Family details

A man is assumed to be 3 years older than his spouse, civil partner or cohabite. A woman is assumed to be 3 years younger than her spouse, civil partner or cohabite.

80% of non-pensioners are assumed to be married / cohabitating at retirement or earlier death.

80% of pensioners are assumed to be married / cohabitating at age 65.

Commutation

Each member is assumed to take cash such that the total cash received (including statutory 3N/80 lump sum) is 80% of the permitted maximum amount permitted of their past service pension entitlements.

Take up of 50/50 scheme

All members are assumed to remain in the scheme which they are in at the valuation date.

Promotional salary increases

Allowance is made for age-related promotional increases.

Expenses

0.5% of Pensionable Pay added to the cost of future benefit accrual.

Method and assumptions used in calculating the cost of future accrual

The cost of future accrual (normal cost) will be calculated using the same actuarial method and assumptions as used to calculate the funding target.

For most employers, the actuarial method to be used is the Projected Unit method with a one year control period. For employers who do not permit new employees to join the Fund, the actuarial method to be used is the Attained Age method. Under both funding methods the salary increases assumed for each member are projected until that member is assumed to leave active service by death, retirement or withdrawal from service.

McCloud/Cost Cap

0.9% of pay has been added to employer contributions based on Fund-specific calculations carried out by the Fund Actuary. This figure has been calculated across the Fund as a whole on the scheduled and subsumption body funding target assuming the following remedy:

- Compensation will apply to members who joined the LGPS before 1 April 2014 (see below).
- Benefits will be the better of those accrued in the 2014 Scheme or those accrued in the 2008 Scheme, backdated to 1 April 2014 (i.e. an 'underpin' approach).
- Compensation will apply to members who retire from active service with immediate pension benefits, through normal health or ill health retirement (this is because transitional protections only applied to members retiring from active service with immediate pension).
- The remedy will not apply to spouses' or dependants' benefits. This is because transitional protections only applied to members' benefits.

The cost is split 0.3% of pay in respect of past service and 0.6% of pay in respect of future service where the past service cost has been spread over a recovery period of 19 years.

GMP indexation/equalisation

There is no allowance for GMP equalisation beyond the extended 'interim' solution announced in January 2018, i.e. for full inflationary increases on GMP to be paid from the Fund for members reaching State Pension Age by 5 April 2021.

Summary of key whole Fund principal financial assumptions used for calculating funding target and cost of future accrual (the “primary contribution rate”) for the 2019 actuarial valuation

Funding target	In service discount rate	Left service discount rate
Scheduled and Subsumption Body	4.25% pa	4.25% pa
Intermediate	3.85% pa	3.75% pa
Ongoing Orphan Body	3.85% pa	1.60% pa

Rate of general pay increases	3.35% pa
Rate of price inflation (RPI)	3.2% pa
Rate of price inflation (CPI)	2.1% pa
Rate of pension increases (on benefits in excess of GMPs)	2.1% pa
Rate of pension increases on post-88 GMPs	1.9% pa
Rate of deferred pension increases	2.1% pa
Rate of GMP increases in deferment	3.35% pa