Financial Scrutiny and Audit Committee
11 February 2014
Agenda Item No 7

Draft 2013 Pension Valuation Results

Report by Head of Finance

Summary:	This report provides members with a summary of the draft 2013 Pension Valuation results, and an overview of changes to the Local Government Pension Scheme due to be implemented from 1 April 2014.
Recommendation:	That the report be noted.

1 Introduction

1.1 The Authority participates in the Norfolk Pension Fund which is part of the Local Government Pension Scheme (LGPS). The Fund is subject to a triennial valuation regime, with the last valuation having been conducted in 2010. The purpose of the valuation is to:

- calculate the funding position of individual employers within the fund; and
- determine the contributions to be paid by employers from 1 April 2014 to 31 March 2017.

1.2 Members should note that the valuation figures are draft at this stage and final figures will be published by 31 March 2013. However, the Fund does not currently anticipate any changes from the draft figures.

2 Draft Valuation Results 2013

2.1 Details of the actuary's valuation process, definitions and assumptions are set out in appendix 1. The draft results for the Broads Authority are set out in appendix 2.

2.2 In particular, section 3 of appendix 2 sets out the valuation results for the Authority including a reconciliation of the movement in the Authority's deficit in the Fund. This has increased from £1,924k in the 2010 valuation to £2,862k at 31 March 2013. Although investment performance has been better than predicted, changes in both the mortality and financial assumptions have led to the increased deficit position. Members will note that in spite of this, the level of funding has only declined slightly (from 86% to 85%), and the Authority remains above average in terms of the funding levels compared against the whole fund (78%).

2.3 The Authority's results are very much in line with the expectations of the actuary at a whole fund level in that funding levels were expected to be slightly lower, and the cash amounts of deficits significantly larger.

2.4 Based on the draft 2013 valuation, the proposed employer contribution rates for 2014/15 to 2016/17 are 15% (this represents no change from the rates applied in the 2010 valuation). The lump-sum deficit contribution increases are set out below.

Table 1 – Annual lump-sum pension deficit contribution

Year	Lump-sum payment £
2013/14	73,000
2014/15	93,000
2015/16	112,000
2016/17	137,000

2.5 The increases in the annual lump-sum payment are in line with expectations and have been taken account of in the Authority's draft budget and financial strategy. The "target" annual lump-sum payment to eliminate the Authority's deficit over a 20 year time frame as calculated by the actuary is £217k. The Authority is classed as a "Tier 1" (long term stable) member of the Fund, which means that the deficit is recovered over a maximum 20 year period and a stabilisation mechanism applied to limit the employer contribution rate variations to a maximum annual movement of +/- 0.5% of pay, so there is no risk of an increase to the full annual contribution in the short term.

2.6 The Fund is also required to produce a Funding Strategy Statement (FSS) which is a summary of the Fund's approach to funding its liabilities. The FSS is subject to consultation at each valuation and the draft FSS is set out at appendix 3 for members' information. The FSS relates to all employers in the Fund. There are no items raised within the draft FSS which officers consider it necessary to respond to in the consultation.

3 Reform of the Local Government Pension Scheme – LGPS 2014

3.1 Changes to the Local Government Pension Scheme (LGPS) are being implemented nationally from 1 April 2014 following the introduction of the Local Government Pension Scheme Regulations 2013. The principle changes to the scheme, when compared to the scheme from 2008, are set out in the table below.

Table 2 – Summary of LGPS changes

	LGPS 2014	LGPS 2008
Basis of Pension	Career Average Revalued Earnings (CARE)	Final Salary
Accrual Rate	1/49th	1/60th

Revaluation Rate	Consumer Prices Index (CPI)	Based on Final Salary
Pensionable Pay	Pay including non-contractual overtime and additional hours for part time staff	Pay excluding non-contractual overtime and non-pensionable additional hours
Contribution Flexibility	Yes, members can pay 50% contributions for 50% of the pension benefit	No
Normal Pension Age	Equal to the individual member's State Pension Age	65
Lump Sum Trade Off	Trade £1 of pension for £12 lump sum	Trade £1 of pension for £12 lump sum
Death in Service Lump Sum	3 x Pensionable Pay	3 x Pensionable Pay
Death in Service Survivor Benefits	1/160th accrual based on Tier 1 ill health pension enhancement	1/160th accrual based on Tier 1 ill health pension enhancement
Ill Health Provision	Tier 1 - Immediate payment with service enhanced to Normal Pension Age Tier 2 - Immediate payment with 25% service enhancement to Normal Pension Age Tier 3 - Temporary payment of pension for up to 3 years	Tier 1 - Immediate payment with service enhanced to Normal Pension Age (65) Tier 2 - Immediate payment with 25% service enhancement to Normal Pension Age (65) Tier 3 - Temporary payment of pension for up to 3 years
Indexation of Pension in Payment	CPI	CPI (RPI for pre-2011 increases)
Vesting Period	2 years	3 months

3.2 Employee contribution rates within the scheme have also been revised as set out below.

Table 3 – LGPS 2008 Employee Contribution Rates

Pay Bands	**LGPS 2008 Contribution Rate**
£0 - £13,700	5.5%
£13,701 - £16,100	5.8%
£16,101 - £20,800	5.9%
£20,801 - £34,700	6.5%
£34,701 - £46,500	6.8%
£46,501 - £87,100	7.2%
More than £87,100	7.5%

Table 4 – LGPS 2014 Employee Contribution Rates

Pay Bands	NEW LGPS 2014 Contribution Rate
Up to £13,500	5.5%
£13,501 - £21,000	5.8%
£21,001 - £34,000	6.5%
£34,001 - £43,000	6.8%
£43,001 - £60,000	8.5%
£60,001 - £85,000	9.9%
£85,001 - £100,000	10.5%
£100,001 - £150,000	11.4%
More than £150,000	12.5%

3.3 The changes to contribution bands results in a more progressive weighting of contributions towards higher earners.

3.4 The reforms to the scheme have been developed through negotiation between the unions, employers and Government, and are intended to:

- ensure a balance between what employees pay and the cost to employers and taxpayers, and
- ensure that the cost of providing public sector pensions remains affordable in the long term.

3.5 The new scheme will not affect the Authority's past service funding position as existing benefits accrued within the LGPS are protected by legislation. The calculation of the future service rate within the 2013 valuation has been based on the benefits that will accrue under the new benefit structure for LGPS 2014.

3.6 The average overall impact of the LGPS 2014 reform is projected to be a slight reduction (around 1.5%) in employer future service costs for the whole of the Fund. Individual employer experience will vary and may see a cost increase where the employer has a higher proportion of the workforce closer to retirement.

4 Summary

4.1 The Authority is required to offer membership of the LGPS to eligible employees as a listed body under Part 1, Schedule 2 of the Local Government Pension Scheme Regulations 2013. Although pension costs represent a small but significant element of the Authority's overall staff expenditure, it is important to recognise that the Authority (and indeed any employer within the scheme) has very limited scope to influence these costs.

4.2 Although the draft valuation figures for 2013 indicate a significant increase in the Authority's cash deficit, it is should be noted that the valuation is a snapshot and it is therefore highly sensitive to both the general assumptions

applied, and the wider economic environment. If economic conditions continue to improve, the results of the next valuation in 2016 could be markedly different. Within the wider LGPS, the Norfolk Pension Fund is both highly regarded and efficient. The Authority's funding level within the Fund is above average and there is a clear strategy for a managed approach to address the Authority's deficit position over the long term.

Background papers: None

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Date of report: 28 January 2014

Broads Plan Objectives: None

Appendices: APPENDIX 1 – Draft Norfolk Pension Fund Employer Results Report
APPENDIX 2 – Draft Valuation Results – Broads Authority
APPENDIX 3 – Draft Funding Strategy Statement

APPENDIX 1

HYMANS ROBERTSON

Norfolk Pension Fund

Employer Results Report: Valuation as at 31 March 2013

November 2013

Gemma Sefton FFA

Fellow of the Institute and Faculty of Actuaries

For and on behalf of Hymans Robertson LLP

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1 Introduction

The Fund Actuary is currently conducting the 31 March 2013 formal valuation of the Norfolk Pension Fund of which you are a participating employer. The Fund is one part of the Local Government Pension Scheme (LGPS). This report is intended to accompany the Results Schedule which sets out your own formal valuation results.

This is a component report of the final aggregate valuation report.

The following Technical Actuarial Standards[1] are applicable in relation to this report and have been complied with where material:

- TAS R – Reporting;
- TAS D – Data;
- TAS M – Modelling; and
- Pensions TAS.

A glossary is contained as Appendix A: please refer to this is you are unfamiliar with any of the terms used in this covering report or the Results Schedule.

What is a formal valuation?

A formal valuation has two main purposes:

- To calculate your funding position within the Fund
- To determine the contributions you will pay to the Fund from 1 April 2014 to 31 March 2017.

This report is intended to help you, as an employer within the Fund, to understand what your funding position means, how it can change and how this will impact on the contributions you pay to the Fund.

[1] Technical Actuarial Standards (TASs) are issued by the Financial Reporting Council (FRC) and set standards for certain items of actuarial work, including the information and advice contained in this report.

2 Your funding position

What is my funding position?

- Past service liability: this is the value that has been placed on the benefits **built up to date** by your employees and ex-employees.
- Asset share: this is the market value of the share of the Fund's assets that have been allocated to you. The Fund Actuary uses a technique known as analysis of surplus to allocate assets to employers at the valuation. This technique utilises the available valuation data to track changes in the employer's surplus or deficit. The items allowed for in the analysis of surplus are set out in Appendix C
- Surplus/deficit: this is the difference between the assets you have and the past service liabilities you are responsible for. If you have more assets than liabilities you have a surplus. If you have fewer assets than past service liabilities then you have a deficit. You are responsible for repaying any deficit to the Fund over an agreed period ("the deficit recovery period").
- Funding level: this is the ratio of your share of the Fund's assets to your past service liabilities.

What will affect my funding position?

Data

A summary of the membership data as supplied to the Fund Actuary is summarised in Section 1 of the Results Schedule. It is the responsibility of the employer to ensure the Fund holds correct data in respect of your current and ex-employees. Incorrect data may impact on your formal valuation results and subsequently the contributions you pay to the Fund.

Actuarial assumptions

The assumptions are agreed between the Fund Actuary and the Administering Authority and are set out in the Fund's Funding Strategy Statement ("FSS").

The financial assumptions are set out in the Results Schedule.

The demographic assumptions are set out in Appendix B.

Experience since the last formal valuation

Your funding position will be affected by the experience of the Fund and your membership over the last 3 years (or date of joining if more recent). This is set out in page 4 of the Results Schedule in the table titled Reconciliation of surplus/deficit

This is explained in Appendix C

What can I do in the future to improve my funding position?

There are some elements of membership experience that employers can control. These are:

- The contributions you pay to the Fund: any contributions you make to the Fund (in addition to the cost of the benefits that are being earned by your employees) will decrease any deficit you have. You will also receive investment returns on any contributions you make.
- Salary increases: the pensionable salary increases awarded to your employees affect the pension received by them in retirement. If you intend to award higher salary increases than have been allowed for in the 2013 valuation assumptions, you may wish to ask the Administering Authority to investigate the impact of this.

- Ill-health early retirements: some Funds monitor ill-health experience and will request additional payments where your ill-health experience has exceeded that allowed for in the valuation calculations. It is also possible to purchase ill-health insurance that will pay the additional cost that arises from an ill-health early retirement. The Funding Strategy Statement will set out your Fund's treatment of ill-health early retirements.

You will find it helpful to speak with the Administering Authority regularly if you are concerned about your funding position or future pension costs. It may be possible to provide an indication of your funding position between formal valuation dates to allow you to monitor how your pensions obligations are changing.

Will the new 2014 scheme benefit structure impact on my funding position?

As all benefits that have been earned to date are protected, there is no change to your *past service* funding position resulting from the new scheme.

3 The contributions you pay to the Fund

How are my valuation contributions calculated?

Employer contributions are normally made up of two elements:

a) the estimated cost of future benefits being built up from year to year, referred to as the "*valuation future service rate*"; plus

b) an adjustment for the difference between the assets built up to date and the value of past service benefits, referred to as the "*deficit recovery repayments*". If there is a deficit then there will be an increase in the employer's contribution; if there is a surplus this may reduce the employer's contribution. Any deficit recovery repayments will aim to return the employer to full funding over an appropriate period (the "deficit recovery period").

The future service rate will depend on the profile of your membership. For example, the rate is higher for older members as there is less time to earn investment returns on the contribution before the member's pension comes into payment.

The methodology for calculating the future service rate will also depend on whether you are open or closed to new entrants. A closed employer will have a higher rate as we must allow for the consequent gradual ageing of the workforce if no new members will join.

There is no guarantee that the amount you pay for future service contributions will be sufficient to meet the cost of the benefits that accrue. The probability that payment of this future service rate over the following one year will be sufficient to fully fund the cost of benefits accruing over the one year period is set out in the Results Schedule. This has been measured at the end of the deficit recovery period (see below).

Similarly, there is no guarantee that the deficit repayment contributions will return you to being fully funded at the end of your deficit recovery period.

The contributions you are being asked to pay are set out in Section 4 of the Results Schedule. These may be different from the valuation contributions described as above. The reasons for any differences are discussed below.

What contributions do I have to pay?

As discussed above, there is no guarantee that the valuation contributions (either the future service component or the deficit recovery repayments) will be sufficient. This is because the cost of benefits to be paid to members now and in the future is uncertain and will not be known until the last payment is made to the last members or their dependants. The Fund actuary makes assumptions about the future in order to assess an appropriate contribution rate but these assumptions are unlikely to be borne out in practice each and every year in the future.

The valuation contributions and the contributions you are being asked to pay are set out in the Results Schedule.

In some cases, the Fund may request that you pay different contributions from the valuation contributions described above. Contributions may vary as a result of the following:

- Stabilisation: this is a mechanism that allows contribution rate changes to be limited and may apply to some employers in the Fund. Please refer to the Funding Strategy Statement for further details on the employers that the Administering Authority have permitted to adopt a "stabilised" contribution strategy

- Future service rate model: for some employers who are not permitted to stabilise, the Fund may request a different level of contributions to be paid. This may be lower or higher than the valuation contribution rate. The rate payable will depend on the probability that the requested contributions will be sufficient to meet either the cost of accruing benefits or to return you to a fully funded position at the end of your deficit recovery period. Further details are provided in Appendix D
- Phasing: the Fund may permit changes in contributions to be phased in over a number of years.

Please refer to the Funding Strategy Statement for your Fund's policies for setting contributions.

The contributions you are asked for and as set out in the Fund's Rates and Adjustment Certificate are a minimum. Any additional contributions you pay to the Fund will have a positive impact on your funding position. The Rates and Adjustments Certificate must be published by 31 March 2014 and applies until 31 March 2017.

Will the new 2014 scheme benefits impact on the contributions I am asked to pay?

As the new scheme takes effect from 1 April 2014, the calculation of the future service rate is determined with reference to the benefits that will accrue under the new benefit structure.

For some employers, this will be less than they would otherwise have been asked to pay.

However, for some employers, the future service rate may be higher than before. This is because members will earn a higher amount of benefit each year ($1/49^{th}$) under the new scheme than they earned before ($1/60^{th}$). Also all members within ten years of retirement will receive the higher of the two benefit structures. Therefore for employers with a large proportion of older members, the new scheme may be more expensive.

The past service adjustment element of the contribution rate is not affected as there is no change in deficit resulting from the new scheme.

How long do I have to pay off the deficit?

This is set out in the Fund's Funding Strategy Statement and varies depending on your circumstances.

The "Deficit repayment contributions" shown in Section 4 of the Results Schedule will show the deficit recovery period which applies to you.

What if I am part of a pool?

If you participate within a pool, all employers in the pool will be asked to pay the same contributions. These contributions may be more or less than you would have paid if you were an individual employer in the Fund.

What if I am planning to leave the Fund?

If you leave the Fund, a "cessation valuation" will be carried out. It will determine whether you have a surplus or deficit, where any deficit will have to be repaid to the Fund. Please refer to your Fund's Funding Strategy Statement for details on how a cessation valuation would be carried out.

If you are planning to leave the Fund soon, you may wish to ask the Fund for an indication of any cessation payment you will be asked to make.

Appendix A – Glossary

Actuarial assumptions/basis	The combined set of assumptions made by the actuary, regarding the future, to calculate the value of **liabilities**. The main assumptions will relate to the **financial assumptions** such as **discount rate**, salary growth, pension increases and **demographic assumptions** such as longevity. More prudent assumptions will give a higher liability value, whereas more optimistic assumptions will give a lower value.
Administering Authority	The council with statutory responsibility for running the Fund, in effect the Fund's "trustees".
Deficit	The shortfall between the assets value and the **liabilities** value. This relates to assets and liabilities built up to date, and ignores the future build-up of pension (which in effect is assumed to be met by future contributions).
Deficit recovery repayment	The part of the employer's annual contribution which relates to past service **deficit** repair.
Demographic assumptions	These assumptions determine when a benefit is paid. The main demographic assumption is the mortality assumption, which determines how long benefits are paid for. Other examples of demographic assumptions are the number of employees that leave the Fund and the number of employees that retire with ill-health benefits
Discount rate	The annual rate at which future assumed cashflows (in and out of the Fund) are discounted to the present day. This is necessary to provide a **liabilities** value which is consistent with the present day value of the assets, to calculate the **deficit**. A lower discount rate gives a higher liabilities value, and vice versa. It is similarly used in the calculation of the **future service rate** and the **common contribution rate**.
Employer	An individual participating body in the Fund, which employs (or used to employ) **members** of the Fund. Normally the assets and **liabilities** values for each employer are individually tracked, together with its **future service rate** at each **valuation**.
Financial assumptions	The main financial assumptions are the discount rate (assumed investment return), the salary increase assumption and the pension increase assumption.
Funding level/position	The ratio of assets value to **liabilities** value. The ideal position is 100%. If it is less than 100% then you have a deficit; if it is more than 100% then you have a surplus.
Future service rate	The actuarially calculated cost of each year's build-up of pension by the current active **members**, excluding members' contributions but including Fund administrative expenses. This is calculated using a chosen set of **actuarial assumptions**.

Liabilities	The actuarially calculated present value of all pension entitlements of all **members** of the Fund, built up to date. This is compared with the present market value of Fund assets to derive the **deficit**. It is calculated on a chosen set of **actuarial assumptions**.
LGPS	The Local Government Pension Scheme, a public sector pension arrangement put in place via Government Regulations, for workers in local government. These Regulations also dictate eligibility (particularly for Scheduled Bodies), members' contribution rates, benefit calculations and certain governance requirements. The LGPS is divided into 101 Funds which map the UK. Each LGPS Fund is autonomous to the extent not dictated by Regulations, e.g. regarding investment strategy, employer contributions and choice of advisers.
Members	The individuals who have built up (and may still be building up) entitlement in the Fund. They are divided into actives (current employee members), deferreds (ex-employees who have not yet retired) and pensioners (ex-employees who have now retired, and dependants of deceased ex-employees).
Pooling	Employers may be grouped together for the purpose of calculating contribution rates, so that their combined membership and asset shares are used to calculate a single contribution rate applicable to all employers in the pool. A pool may still require each individual employer to ultimately pay for its own share of **deficit**, or (if formally agreed) it may allow **deficits** to be passed from one employer to another.
Profile	The profile of an employer's membership or liability reflects various measurements of that employer's **members**, i.e. current and former employees. This includes: the proportions which are active, deferred or pensioner; the average ages of each category; the varying salary or pension levels; the lengths of service of active members vs. their salary levels, etc. A membership (or liability) profile might be measured for its **maturity** also.
Stabilisation	Any method used to smooth out changes in employer contributions from one year to the next. This is very broadly required by the LGPS Regulations, but in practice is particularly employed for large stable employers in the Fund. Different methods may involve: probability-based modelling of future market movements; longer deficit recovery periods; higher discount rates; or some combination of these.
Total valuation contribution rate	The employer's contribution rate, including both **future service rate** and **deficit recovery repayment**, which would be calculated on the standard **actuarial basis**, before any allowance for **stabilisation** or other agreed adjustment.
Valuation	An actuarial investigation to calculate the liabilities, future service contribution rate and common contribution rate for a Fund, and usually individual employers too. This is normally carried out in full every three years (last done as at 31 March 2013), but can be approximately updated at other times. The assets value is based on market values at the valuation date, and the liabilities value and contribution rates are based on long term bond market yields at that date also.

Appendix B – Demographic assumptions

Death in Service

Age	Incidence per 1000 active members per annum			
	Male officers and Post 98	Male Manuals	Female officers and Post 98	Female Manuals
	Death	Death	Death	Death
20	0.21	0.27	0.12	0.15
25	0.21	0.27	0.12	0.15
30	0.26	0.32	0.18	0.22
35	0.30	0.37	0.30	0.37
40	0.51	0.64	0.48	0.60
45	0.85	1.07	0.77	0.97
50	1.36	1.71	1.13	1.42
55	2.13	2.68	1.49	1.87
60	3.83	4.82	1.90	2.39
65	6.38	8.03	2.44	3.07

Ill Health Early Retirements

Tier 1

Age	Incidence for 1000 active members per annum							
	Male Officers & Post 98 Males		Male Manuals		Female Officers & Post 98 Females		Female Manuals	
	Ill Health		Ill Health		Ill Health		Ill Health	
	FT	PT	FT	PT	FT	PT	FT	PT
20	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
25	0.00	0.00	0.60	0.60	0.15	0.11	0.79	0.79
30	0.00	0.00	1.11	1.11	0.20	0.15	1.15	1.15
35	0.15	0.11	1.66	1.66	0.40	0.30	1.58	1.58
40	0.25	0.19	2.42	2.42	0.60	0.45	2.30	2.30
45	0.55	0.42	3.33	3.33	0.81	0.60	3.02	3.02
50	1.41	1.06	4.94	4.94	1.51	1.13	4.03	4.03
55	5.53	4.15	11.69	11.69	5.61	4.20	10.83	10.83
60	9.73	7.30	18.74	18.74	11.89	8.92	19.05	19.05
65	18.48	13.86	36.12	36.12	21.37	16.03	36.12	36.12

Tier 2

Age	Incidence for 1000 active members per annum							
	Male Officers & Post 98 Males		Male Manuals		Female Officers & Post 98 Females		Female Manuals	
	Ill Health		Ill Health		Ill Health		Ill Health	
	FT	PT	FT	PT	FT	PT	FT	PT
20	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
25	0.00	0.00	0.64	0.64	0.16	0.12	0.84	0.84
30	0.00	0.00	1.18	1.18	0.21	0.16	1.22	1.22
35	0.16	0.12	1.77	1.77	0.43	0.32	1.68	1.68
40	0.27	0.20	2.57	2.57	0.64	0.48	2.45	2.45
45	0.59	0.44	3.53	3.53	0.86	0.64	3.21	3.21
50	1.90	1.42	6.65	6.65	2.03	1.53	5.43	5.43
55	4.27	3.20	9.03	9.03	4.33	3.25	8.37	8.37
60	3.66	2.75	7.05	7.05	4.48	3.36	7.17	7.17
65	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Tier 3

Age	Incidence for 1000 active members per annum							
	Male Officers & Post 98 Males		Male Manuals		Female Officers & Post 98 Females		Female Manuals	
	Ill Health		Ill Health		Ill Health		Ill Health	
	FT	PT	FT	PT	FT	PT	FT	PT
20	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
25	0.00	0.00	0.48	0.38	0.09	0.07	0.55	0.44
30	0.09	0.07	0.77	0.62	0.15	0.12	0.77	0.61
35	0.12	0.10	1.16	0.93	0.30	0.24	1.11	0.88
40	0.21	0.17	1.61	1.29	0.39	0.31	1.53	1.22
45	0.48	0.38	2.32	1.86	0.62	0.50	1.96	1.56
50	0.26	0.21	0.68	0.54	0.24	0.20	0.58	0.46
55	0.37	0.30	0.77	0.61	0.45	0.36	0.76	0.61
60	0.21	0.17	0.42	0.33	0.25	0.20	0.42	0.33
65	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

Withdrawal

Less than 2 years' service

Age	Incidence for 1000 active members per annum											
	Male Officers Withdrawals		Male Manuals Withdrawals		Female Officers Withdrawals		Female Manuals Withdrawals		Post 98 Males Withdrawals		Post 98 Females Withdrawals	
	FT	PT	FT	PT	FT	PT	FT	PT	FT	PT	FT	PT
20	304.04	506.74	304.04	506.74	288.39	400.55	288.39	400.55	557.41	1000.00	384.52	640.87
25	200.83	334.72	201.20	335.01	194.07	269.50	194.43	269.79	368.19	736.38	258.74	431.17
30	142.53	237.46	143.05	237.91	162.69	225.89	163.17	226.27	261.24	522.40	216.89	361.38
35	111.38	185.51	112.17	186.19	140.45	194.94	141.07	195.43	204.11	408.11	187.19	311.79
40	89.71	149.31	90.77	150.23	116.92	162.22	117.80	162.92	164.33	328.47	155.80	259.40
45	73.64	122.28	75.03	123.55	96.49	133.73	97.50	134.54	134.71	268.98	128.49	213.73
50	56.96	94.68	57.28	95.02	73.34	101.75	73.60	101.96	104.26	208.28	97.73	162.71
55	49.47	82.09	49.77	82.44	56.73	78.59	56.97	78.78	90.46	180.57	75.53	125.58
60	29.97	49.75	30.13	49.94	26.40	36.55	26.52	36.65	54.81	109.43	35.13	58.39

More than 2 years' service

Age	Incidence for 1000 active members per annum											
	Male Officers Withdrawals		Male Manuals Withdrawals		Female Officers Withdrawals		Female Manuals Withdrawals		Post 98 Males Withdrawals		Post 98 Females Withdrawals	
	FT	PT	FT	PT	FT	PT	FT	PT	FT	PT	FT	PT
20	119.85	199.76	119.85	199.76	113.69	157.90	113.69	157.90	219.73	439.46	151.58	252.63
25	79.17	131.95	79.31	132.06	76.50	106.24	76.64	106.35	145.14	290.28	101.99	169.97
30	56.18	93.60	56.39	93.78	64.13	89.05	64.32	89.20	102.98	205.93	85.50	142.46
35	43.90	73.12	44.22	73.40	55.37	76.84	55.61	77.04	80.46	160.88	73.79	122.91
40	35.36	58.85	35.79	59.22	46.09	63.95	46.44	64.22	64.78	129.48	61.42	102.26
45	29.03	48.18	29.59	48.71	38.04	52.72	38.44	53.04	53.10	106.03	50.65	84.25
50	22.45	37.31	22.58	37.46	28.91	40.11	29.01	40.19	41.10	82.10	38.52	64.14
55	19.50	32.35	19.62	32.50	22.36	30.98	22.46	31.06	35.66	71.18	29.77	49.50
60	11.82	19.60	11.88	19.69	10.41	14.41	10.46	14.45	21.61	43.14	13.85	23.02

Promotional salary scale

Age	Promotional Salary Scales							
	Male Officers & Post 98 Males		Male Manuals		Female Officers & Post 98 Females		Female Manuals	
	FT	PT	FT	PT	FT	PT	FT	PT
20	100	100	100	100	100	100	100	100
25	135	116	100	100	118	105	100	100
30	169	134	100	100	137	111	100	100
35	192	146	100	100	151	116	100	100
40	208	153	100	100	163	121	100	100
45	222	154	100	100	166	122	100	100
50	236	154	100	100	166	122	100	100
55	239	154	100	100	166	122	100	100
60	239	154	100	100	166	122	100	100
65	239	154	100	100	166	122	100	100

Longevity assumptions	31 March 2013
Longevity - baseline	Vita curves
Longevity - improvements	
CMI Model version used	CMI_2010
Starting rates	CMI calibration based on data from Club Vita using the latest available data as at December 2011.
Long term rate of improvement	Period effects: 1.25% p.a. for men and women. Cohort effects: 0% p.a. for men and for women.
Period of convergence	Period effects: CMI model core values i.e. 10 years for ages 50 and below and 5 years for those aged 95 and above, with linear transition to 20 years for those aged between 60 and 80. Cohort effects: CMI core i.e. 40 years for those born in 1947 or later declining linearly to 5 years for those born in 1912 or earlier.
Proportion of convergence remaining at mid point	50%

We have suggested a longevity improvement assumption based on the latest industry standard and combined information from our longevity experts in Club Vita. The start point for the improvements has been based on observed death rates in the Club Vita data bank over the period.

In the short term we have assumed that the ‘cohort effect’ of strong improvements in life expectancy currently being observed amongst a generation born around the early and mid 1930s will start to tail off, resulting in life expectancy increasing less rapidly than has been seen over the last decade or two. This is known as ‘peaked’.

In the long term (post age 70) we have assumed that increases in life expectancy will stabilise at a rate of increase of 1 year per decade for men and women. This is equivalent to assuming that longer term mortality rates will fall at a rate of 1.25% p.a. for men and women.

However, we have assumed that post age 90 improvements in mortality are hard to achieve, declining between ages 90 and 120 so that no improvements are seen at ages 120 and over. The initial rate of mortality is assumed to decline steadily above age 98.

Commutation assumptions and take – up of the 50:50 scheme

These assumptions are set out in the Results Schedule.

Appendix C – Reconciliation of Surplus/Deficit

Interest on the surplus/deficit	A surplus or deficit in the Fund will grow in line with the Fund Actuary's expectation of future investment performance (the discount rate).
Investment returns more/less than expected	The Fund Actuary makes an assumption about the Fund's investment return each year (the discount rate). Where the Fund's actual returns have been greater than this, this will have a positive effect on the funding position. If the Fund's actual return each year is less than the discount rate, this will have a negative effect.
Contributions greater than the cost of accrual	Any contributions you pay to the Fund in excess of the assessed cost of the benefits that have been earned by your employees will have a positive effect on the funding position.
Salary increases more/less than expected	The Fund Actuary makes an assumption about the level of future salary increases. If you have awarded salary increases that are higher over the last three years, this will have a negative effect on your funding position. If you have awarded lower salary increases, this will have a positive effect on your funding position. **You should be aware of the level of salary increases that the Fund Actuary has assumed in their calculations and consider the pension costs if you intend to award higher salary increases to your employees.**
Pension increases more/less than expected	The Fund Actuary makes an assumption for the expected levels of the Consumer Price Index. This is the expected level of future pension increases for deferred and pensioner members. Over the period from 2010 to 2013, actual pension increases have been slightly higher than assumed. This has a small negative impact on the funding position.
Ill-health retirement strain/contributions paid	The Fund Actuary makes an allowance for people to retire early with ill-health benefits. Ill-health early retirements cost more than normal retirements. If fewer members than expected have retired on ill-health grounds, this will have a positive impact on your funding position. If more members than expected have retired on ill-health then this will have a negative

	impact on your valuation results. You may have been asked to make a payment towards the cost of ill-health early retirements or you may have ill-health insurance. Any payments you have made to the Fund will have a positive effect on your funding position.
Redundancy/ efficiency early retirement strain / contributions paid	The Fund Actuary is supplied with data for all other early retirements. The cost of each early retirement is calculated and will have a negative impact on the funding position. However, any early retirement contributions you have made to the Fund will have a positive effect on your funding position. Due to differences in the way these calculations are carried out, the payment you have made to the Fund may be more or less than the actuarially assessed strain cost.
Early leavers more/less than expected	At the 2010 valuation, an assumption was made about the number of members who would withdraw from the Fund. Early leavers' benefits usually cost less than normal retirements. The Fund Actuary compares the actual number of leavers to the expected number of leavers for the last three years. Where this is more than expected, this will have a positive impact on the funding position. Where this is less than expected, this will have a negative impact on the funding position.
Pensioner deaths more/less than expected	At the 2010 valuation, an assumption was made about how long members would live for. Where pensioners have lived for longer than expected, this will have a negative impact on your funding position. Where more pensioners have died than expected, this would have a positive impact on your funding position.
Commutation higher/lower than expected	An assumption was made at the 2010 valuation for the amount of pension that a retiring member would choose to commute to receive an additional lump sum. Usually a lump sum costs less than the valuation assessment of the pension commuted. Where members commute a higher amount of pension than expected, this will have a positive impact on the funding position, and vice versa.

Change in demographic assumptions	At each valuation the Fund Actuary performs an experience analysis to compare all demographic assumptions with those assumed at the previous valuation. The demographic assumptions are then altered for the following valuation to more closely reflect what has happened. The impact of the change in these assumptions will depend on the profile of your own membership data.
Change in mortality assumptions	Similarly to the demographic assumptions, the mortality (i.e. life expectancy) assumption is altered at each valuation to reflect more up to date experience. The impact of the change in these assumptions will depend on the profile of your own membership data, and the assumption adopted at the last formal valuation.
Change in financial assumptions	Financial assumptions are derived with reference to current market conditions at each valuation date. The net discount rate (the difference between the discount rate and the salary or pension increase assumption) has an impact on the value placed on the benefits earned to date ("the liabilities"). A smaller net discount rate leads to a higher liability value.
Profit or loss on bulk transfers	If you have been involved in any bulk transfers, there may be a profit or a loss if the value of assets you received (or paid) is different from the value of liabilities you assumed (or transferred). This applies to both transfers between Funds and transfers to/from employers within the Fund. Any transfers that occur on a "fully funded" basis have no impact on the funding position of an employer.
Other experience items	Based on the data available to the Fund Actuary, it is not possible to analyse the impact of all experience that will affect your funding position. As the Fund has a single pot of assets, the Fund Actuary must allocate these assets to each employer. Any difference between the sum of the employers assets and the whole Fund assets is allocated between employers (pro-rated based on the employers liabilities).

Appendix D – Technical appendix for contribution modeller

In order to assess the likelihood of the employer's section of the Fund achieving full funding we have carried out stochastic asset liability modelling that takes into account the main characteristics and features of the employer's share of the Fund's assets and liabilities.

The Results Schedule sets out the probability that the valuation future service rate is sufficient to pay for the benefit that is accrued the following year. The probability is derived using the contribution modeller.

The following sections provide more detail on the background to the modelling.

Cash flows and asset liability model

In projecting forward the evolution of each employer's section of the Fund, we have used estimated cash flows. These cashflows have been generated using approximate methods, including the use of generic model points based on sample members. The demographic assumptions underlying the model point cashflows are consistent with a typical set of assumptions adopted by Hymans Robertson LGPS clients for the 2013 formal valuation. The cashflows do not make any allowance for future new joiners to the Fund.

We do not allow for any variation in actual experience away from the demographic assumptions underlying the cash flows. Variations in demographic assumptions (and experience relative to those assumptions) can result in significant changes to the funding level and contribution rates. We allow for variations in inflation (RPI or CPI as appropriate), inflation expectations (RPI or CPI as appropriate), interest rates, yield curves and asset class returns. Cash flows into and out of the Scheme are projected forward in annual increments and are assumed to occur in the middle of each Scheme year.

These cashflows, and the employer's assets, are projecting forward using stochastic projections of asset returns and economic factors such as inflation and bond yields. These projections are provided by HRAM, our (proprietary) stochastic asset model, which is discussed in more detail below. In allowing for the simulated economic scenarios, we have used suitable approximations for updating the projected cash flows. The nature of the approximations is such that the major financial and investment risks can be broadly quantified.

When placing a value on the liabilities in future, we have assumed that the Actuary to the Fund will make his or her calculations using broadly the same methodology as that currently used. Note that this is a source of uncertainty that we have not attempted to measure in the model.

When projecting forward the assets, we have derived a proxy for the Fund's investment strategy by simplifying their current benchmark into growth (UK equity) and non-growth (index-linked gilts) allocations, and modelling this simplified strategy. Investment strategies are assumed to be rebalanced annually.

We have assumed that all contributions are made and not varied throughout the period of projection irrespective of the funding position. In practice the contributions are likely to vary especially if the funding level changes significantly. Investment strategy may also change with significant changes in funding level, but we have not considered the impact of this.

As with all modelling, the results are dependent on the model itself, the calibration of the model and the various approximations and estimations used. These processes involve an element of subjectivity. No inferences should be drawn from the modelling results other than those confirmed by us in writing.

Asset returns

The outcomes of our analysis depend significantly on HRAM, our (proprietary) stochastic asset model. This type of model is known as an economic scenario generator and uses probability distributions to project a range of possible outcomes for the future behaviour of asset returns and economic variables. Some of the parameters of the model are dependent on the current state of financial markets and are updated each month (for example, the current level of equity market volatility) while other more subjective parameters do not change with different calibrations of the model.

Key subjective assumptions are the average excess equity return over the risk free asset (tending to approximately 3% p.a. as the investment horizon is increased), the volatility of equity returns (approximately 18% p.a. over the long term) and the level and volatility of yields, credit spreads, inflation and expected (breakeven) inflation, which affect the projected value placed on the liabilities and bond returns. The market for CPI linked instruments is not well developed and our model for expected CPI in particular may be subject to additional model uncertainty as a consequence. The output of the model is also affected by other more subtle effects, such as the correlations between economic and financial variables.

Our expectation (i.e. the average outcome from the range of possible future outcomes) is that long term real interest rates will rise from their current low levels. Higher long-term yields in the future will mean a lower value placed on liabilities and therefore our average outcome will show, all other things being equal, an improvement in the current funding position (because of the mismatch between assets and liabilities). The mean reversion in yields also affects expected bond returns.

While the model allows for the possibility of scenarios that would be extreme by historical standards, including very significant downturns in equity markets, large systemic and structural dislocations are not captured by the model. Such events are unknowable in effect, magnitude and nature, meaning that the most extreme possibilities are not necessarily captured within the distributions of results.

Given the context of this modelling, we have not undertaken any sensitivity analysis to assess how different results might be with alternative calibrations of the economic scenario generator.

Median rates of Return and Volatilities

The following figures have been calculated using 5,000 simulations of the Hymans Robertson Asset Model (HRAM), calibrated using market data as at 31 March 2013. The absolute expected returns show the geometric annualised averages over a range of time horizons and the absolute volatilities quoted are the first year's standard deviations. All returns are shown net of fees.

It is important to be aware that the volatilities shown are only the first year's volatilities and should only be used as such. The probability distributions for different asset classes are complex and attempting to extrapolate this first year volatility over a longer time period will almost certainly result in significant errors.

	UK Equity	Index Linked Gilts (medium-dated)
Expected rate of return (p.a.)		
- 1 year	3.7%	-0.3%
- 5 year	4.3%	0.0%
- 10 year	5.2%	1.0%
- 15 year	5.8%	1.8%
- 20 year	6.2%	2.3%
Volatility	16.0%	6.0%

Please also note that whilst we comment that the returns shown are “expected”, this simply identifies the level at which 50% of all possible outcomes will be above and 50% will be below – this does not mean that the return quoted is in any way the “most likely” outcome.

The current calibration of the model indicates that a period of outward yield movement is expected. For example, over the next 10 years our model expects the 17 year maturity annualised real (nominal) interest rate to rise from -0.5% (3.1%) to 1.2% (4.4%).

31 March 2013 Formal Valuation - Draft Results

ATTENTION
The results in this Schedule should be read in conjunction with the Employer Results Report. The method, assumptions, reliances and limitations are described in this document. The restrictions set out in the report on the disclosure to any third party apply equally to this Results Schedule.

Fund	Norfolk Pension Fund
Administering Authority	Norfolk County Council
Employer	Not applicable
Pool	Broads Pool
CPX Code/Pool Name	Broads Pool
Open/Closed	Open
Employer Type	Pool

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Gemma Sefton
For and on behalf of Hymans Robertson LLP

21 November 2013

Section 1 - Pool Data

Pool membership statistics

	Number		Average Age		Duration
	31 Mar 2010	31 Mar 2013	31 Mar 2010	31 Mar 2013	31 Mar 2013
Actives	125	119	51.3	52.5	22.4
Deferred Pensioners	65	88	49.7	50.3	23.3
Pensioners	58	69	68.2	65.6	12.3

Average age is weighted by liability

The average duration of liabilities based on the valuation assumption is 19.6 years.

	Actual Pay / Pension p.a. (£000)		Average Pay / Pension (£)	
	31 Mar 2010	31 Mar 2013	31 Mar 2010	31 Mar 2013
Actives	2,841	2,677	22,729	22,500
Deferred Pensioners	137	215	2,107	2,449
Pensioners	240	338	4,144	4,906

	FTE Pay (£000)	Average Service 80ths	Average Service 60ths	Average Service 80ths	Average Service 60ths
	31 Mar 2013	31 Mar 2010	31 Mar 2010	31 Mar 2013	31 Mar 2013
Active Males	1,886	14.3	1.8	10.9	2.1
Active Females	1,114	11.3	2.1	8.0	1.9
Total	3,000	13.1	1.9	9.0	2.0

Average service is weighted by salary

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Pool membership movements since last valuation

	Actual	Expected	Difference
Early Leavers	31	27	14%
Ill Health Retirements	3	2	50%
Early Retirements	5	-	100%
£000s	Actual	Expected	Difference
Amounts of Pension Ceasing	51	23	117%

Cashflow data

£000s	Employer contributions	Employee contributions	Benefits paid	Net cashflow
1 April 2010 - 31 March 2011	453	196	278	371
1 April 2011 - 31 March 2012	433	181	431	183
1 April 2012 - 31 March 2013	461	186	400	247

Investment returns

	Actual	Expected
From 1 April 2010 to 31 March 2013	23.4%	19.4%

Section 2 - Assumptions

Financial assumptions

	31 Mar 2010 £(000)	31 Mar 2013 £(000)
Pre-retirement Discount rate	6.1%	4.6%
Post-retirement Discount rate	6.1%	4.6%
Salary increases	5.3%*	3.3%
Pension increases	3.3%	2.5%

*Salary increases are assumed to be 1% until 31 March 2013 then the long term rate shown thereafter.

Mortality

As the fund is a member of Club Vita, the baseline mortality assumptions are a bespoke set of Vita Curves that are tailored to fit the membership profile of the fund.

We have also allowed for future improvements in mortality based on the CMI 2010 model assuming improvements have peaked, long term improvements of 1.25% p.a., with declining mortality for over 90s.

Demographic assumptions

Future retirements are assumed to commute pension into tax-free cash up to 50% of HMRC limits for service to 31 March 2008 and 75% for service thereafter.

We have assumed that there is a 10% probability that members will opt to join the 50:50 scheme.

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Full details of the assumptions used are detailed in the Employer Results Report

Section 3 - Pool Valuation Results

Pool valuation results

	31 Mar 2010 £(000)	31 Mar 2013 £(000)
Past service liabilities		
Active members	8,127	9,623
Deferred pensioners	2,189	3,849
Pensioners	3,294	5,586
Total	**13,610**	**19,058**
Asset share	**11,686**	**16,196**
Surplus / (deficit)	**(1,924)**	**(2,862)**
Funding level	**86%**	**85%**

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Reconciliation of surplus / (deficit)

		£(000)	£(000)
Surplus / (deficit) at last valuation			**(1,924)**
Interest on deficit		(385)	
Expected investment returns	19.4%		
Actual investment returns	23.4%		
Investment returns greater than expected		553	
Contributions greater than cost of accrual		98	
Expected Salary increases p.a.	1.7%		
Actual Salary increases p.a.	1.3%		
Salary increases less than expected		94	
Expected Pension increases (p.a.)	3.3%		
Actual Pension increases (p.a.)	3.5%		
Pension increases more than expected		(41)	
Ill-health retirement strain		(17)	
Ill-health contributions paid		-	
Redundancy / efficiency early retirement strain		(65)	
Early retirement contributions paid / payable		33	
Early leavers more than expected		6	
Pensioner deaths more than expected		370	
Commutation lower than expected		(29)	
Change in demographic assumptions		(9)	
Change in mortality assumptions		(246)	
Change in financial assumptions		(1,550)	
Impact of Bulk transfers		-	
Other experience items		249	
Surplus / (deficit) at this valuation			**(2,862)**

Section 4 - Pool Contribution Rates

Future service rate results

	% of payroll
Valuation future service rate as at 31 March 2013*	**20.4%**
Probability that valuation future service rate is enough to pay for benefit accrued**	**78.5%**

*The future service rate is the cost of new benefits being accrued by active members. The future service rate includes an allowance of 0.4% for expenses.

**Please see the Employer Results Report for a full explanation of this probability

Contribution rates exclude employee contributions. The average employee contribution rate is 6.6%.

Deficit recovery repayment results

	% of payroll		Monetary amount £(000) p.a.
Valuation deficit repayment contributions Spread over 20 years	**6.0%**	or	**217**

Total valuation contribution rate results

	% of payroll		Monetary amount £(000) p.a.
Total valuation rate as at 31 March 2013	**20.4%**	plus	**217**

Proposed Contribution rates for the next three years

	% of payroll		Monetary amount £(000) p.a.
Contributions in payment 2013/2014	**15.0%**	plus	**73**
Proposed certified rates for the year ending			
31 March 2015	**15.0%**	plus	**93**
31 March 2016	**15.0%**	plus	**112**
31 March 2017	**15.0%**	plus	**137**

The proposed contribution rates are after a stabilisation overlay has been applied. Further details about this overlay can be found in the Funding Strategy Statement.

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APPENDIX 3

HYMANS ROBERTSON

Norfolk Pension Fund

DRAFT Funding Strategy Statement

Gemma Sefton

Fellow of the Institute and Faculty of Actuaries

For and on behalf of Hymans Robertson LLP

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1 Introduction

1.1 What is this document?

This is the Funding Strategy Statement (FSS) of the Norfolk Pension Fund ("the Fund"), which is administered by Norfolk County Council, ("the Administering Authority").

It has been prepared by the Administering Authority in collaboration with the Fund's actuary, Hymans Robertson LLP, and after consultation with the Fund's employers and investment adviser. It is effective from TBC.

1.2 What is the Norfolk Pension Fund?

The Fund is part of the national Local Government Pension Scheme (LGPS). The LGPS was set up by the UK Government to provide retirement and death benefits for local government employees, and those employed in similar or related bodies, across the whole of the UK. The Administering Authority runs the Norfolk Pension Fund, to make sure it:

- receives the proper amount of contributions from employees and employers, and any transfer payments;
- invests the contributions appropriately, with the aim that the Fund's assets grow over time with investment income and capital growth;
- uses the assets to pay Fund benefits to the members (as and when they retire, for the rest of their lives), and to their dependants (as and when members die), as defined in the LGPS Regulations. Assets are also used to pay transfer values and administration costs.

The roles and responsibilities of the key parties involved in the management of the Fund are summarised in Appendix B.

1.3 Why does the Fund need a Funding Strategy Statement?

Employees' benefits are guaranteed by the LGPS Regulations, and do not change with market values or employer contributions. Investment returns will help pay for some of the benefits, but probably not all, and certainly with no guarantee. Employees' contributions are fixed in those Regulations also, at a level which covers only part of the cost of the benefits.

Therefore, employers need to pay the balance of the cost of delivering the benefits to members and their dependants.

The FSS focuses on how employer liabilities are measured, the pace at which these liabilities are funded, and how employers or pools of employers pay for their own liabilities. This statement sets out how the Administering Authority has balanced the conflicting aims of:

- affordability of employer contributions,
- transparency of processes,
- stability of employers' contributions, and
- prudence in the funding basis.

There are also regulatory requirements for an FSS, as given in Appendix A.

The FSS is a summary of the Fund's approach to funding its liabilities, and this includes reference to the Fund's other policies; it is not an exhaustive statement of policy on all issues. The FSS forms part of a framework of which includes:

- the LGPS Regulations;

- the Rates and Adjustments Certificate (confirming employer contribution rates for the next three years) which can be found in an appendix to the formal valuation report;
- the Fund's approach to admissions, cessations and bulk transfers;
- actuarial factors for valuing individual transfers, early retirement costs and the costs of buying added service; and
- the Fund's Statement of Investment Principles (see Section 4).

1.4 How does the Fund and this FSS affect me?

This depends who you are:

- a member of the Fund, i.e. a current or former employee, or a dependant: the Fund needs to be sure it is collecting and holding enough money so that your benefits are always paid in full;
- an employer in the Fund (or which is considering joining the Fund): you will want to know how your contributions are calculated from time to time, that these are fair by comparison to other employers in the Fund, and in what circumstances you might need to pay more. Note that the FSS applies to all employers participating in the Fund;
- an Elected Member whose council participates in the Fund: you will want to be sure that the council balances the need to hold prudent reserves for members' retirement and death benefits, with the other competing demands for council money;
- a Council Tax payer: your council seeks to strike the balance above, and also to minimise cross-subsidies between different generations of taxpayers.

1.5 What does the FSS aim to do?

The FSS sets out the objectives of the Fund's funding strategy, such as:

- to ensure the long-term solvency of the Fund, using a prudent long term view. This will ensure that sufficient funds are available to meet all members'/dependants' benefits as they fall due for payment;
- to ensure that employer contribution rates are reasonably stable where appropriate;
- to minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return (**NB** this will also minimise the costs to be borne by Council Tax payers);
- to reflect the different characteristics of different employers in determining contribution rates. This involves the Fund having a clear and transparent funding strategy to demonstrate how each employer can best meet its own liabilities over future years; and
- to use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations.

1.6 How do I find my way around this document?

In Section 2 there is a brief introduction to some of the main principles behind funding, i.e. deciding how much an employer should contribute to the Fund from time to time.

In Section 3 we outline how the Fund calculates the contributions payable by different employers in different situations.

In Section 4 we show how the funding strategy is linked with the Fund's investment strategy.

In the Appendices we cover various issues in more detail if you are interested:

A. the regulatory background, including how and when the FSS is reviewed,

B. who is responsible for what,

C. what issues the Fund needs to monitor, and how it manages its risks,

D. some more details about the actuarial calculations required,

E. the assumptions which the Fund actuary currently makes about the future,

F. a glossary explaining the technical terms occasionally used here.

If you have any other queries please contact Alex Younger, Investment & Actuarial Services Manager in the first instance at e-mail address alexander.younger@norfolk.gov.uk.

2 Basic Funding issues

(More detailed and extensive descriptions are given in Appendix D).

2.1 How does the actuary calculate a contribution rate?

Employer contributions are normally made up of two elements:

a) the estimated cost of future benefits being built up from year to year, referred to as the "*future service rate*"; plus

b) an adjustment for the difference between the assets built up to date and the value of past service benefits, referred to as the "*past service adjustment*". If there is a deficit the past service adjustment will be an increase in the employer's total contribution; if there is a surplus there may be a reduction in the employer's total contribution. Any past service adjustment will aim to return the employer to full funding over an appropriate period (the "deficit recovery period").

2.2 How is a deficit (or surplus) calculated?

An employer's "funding level" is defined as the ratio of:

- the market value of the employer's share of assets, to
- the value placed by the actuary on the benefits built up to date for the employer's employees and ex-employees (the "liabilities"). The Fund actuary agrees with the Administering Authority the assumptions to be used in calculating this value.

If this is less than 100% then it means the employer has a shortfall, which is the employer's deficit; if it is more than 100% then the employer is said to be in surplus. The amount of deficit or shortfall is the difference between the asset value and the liabilities value.

A larger deficit will give rise to higher employer contributions. If a deficit is spread over a longer period then the annual employer cost is lower than if it is spread over a shorter period. Note; interest is payable on any deficit until it is repaid in full.

2.3 How are contribution rates calculated for different employers?

The Fund's actuary is required by the Regulations to report the *Common Contribution Rate*, for all employers collectively at each triennial valuation, combining items (a) and (b) above. This is based on actuarial assumptions about the likelihood, size and timing of benefit payments to be made from the Fund in the future, as outlined in Appendix E.

The Fund's actuary is also required to adjust the *Common Contribution Rate* for circumstances specific to each individual employer. The sorts of specific circumstances which are considered are discussed in Section 3. It is this adjusted contribution rate which the employer is actually required to pay, and the rates for all employers are shown in the Fund's Rates and Adjustments Certificate.

In effect, the *Common Contribution Rate* is a notional quantity, as it is unlikely that any employer will pay that exact rate. Separate future service rates are calculated for each employer together with individual past service adjustments according to employer-specific circumstances.

Details of the outcome of the Actuarial Valuation as at 31 March 2013 can be found in the formal valuation report dated TBC, including an analysis at Fund Level of the *Common Contribution Rate*. Further details of individual employer contribution rates can also be found in the formal report.

2.4 What else might affect the employer's contribution?

Employer covenant and likely term of membership are also considered when setting contributions: more details are given in Section 3.

For some employers it may be agreed to pool contributions, see 3.4.

Any costs of non ill-health early retirements must be paid by the employer, see 3.6.

Any costs of salary increases above that assumed at the formal valuation must be paid by the employer, see Appendix G.

If an employer is approaching the end of its participation in the Fund then its contributions may be amended appropriately, so that the assets meet (as closely as possible) the value of its liabilities in the Fund when its participation ends.

Employers' contributions are expressed as minima, with employers able to pay contributions at a higher rate. If higher contributions are paid into the Fund these will be taken into account by the Fund Actuary at subsequent valuations.

2.5 What different types of employer participate in the Fund?

Historically the LGPS was intended for local authority employees only. However over the years, with the diversification and changes to delivery of local services, many more types and numbers of employers now participate. There are currently more employers in the Fund than ever before, a significant part of this being due to new academies established outside of the Local Education Authority.

In essence, participation in the LGPS is open to public sector employers providing some form of service to the local community. Whilst the majority of members will be local authority employees (and ex-employees), the majority of participating employers are those providing services in place of (or alongside) local authority services: academy schools, contractors, housing associations, charities, etc.

The LGPS Regulations define various types of employer as follows:

Scheduled bodies - councils, and other specified employers such as academies and further education establishments. These must provide access to the LGPS in respect of their employees who are not eligible to join another public sector scheme (such as the Teachers Scheme). These employers are so-called because they are specified in a schedule to the LGPS Regulations.

It is now possible for Local Education Authority schools to convert to academy status, and for other forms of school (such as Free Schools) to be established under the academies legislation. All such academies, as employers of non-teaching staff, become separate new employers in the Fund. As academies are defined in the LGPS Regulations as "Scheduled Bodies", the Administering Authority has no discretion over whether to admit them to the Fund, and the academy has no discretion whether to continue to allow its non-teaching staff to join the Fund.

Designating employers - employers such as town and parish councils are able to participate in the LGPS via resolution (and the Fund cannot refuse them entry where the resolution is passed). These employers can designate which of their employees are eligible to join the scheme.

Other employers are able to participate in the Fund via an admission agreement, and are referred to as 'admission bodies'. These employers are generally those with a "community of interest" with another scheme employer – **community admission bodies** ("CAB") or those providing a service on behalf of a scheme employer – **transferee admission bodies** ("TAB").

CABs will include housing associations and charities, TABs will generally be contractors. The Fund is able to set its criteria for participation by these employers and can refuse entry if the requirements as set out in the Fund's admissions policy are not met.

2.6 How does the Fund recognise that contribution levels can affect council and employer service provision, and council tax?

The Administering Authority and the Fund actuary are acutely aware that, all other things being equal, a higher contribution required to be paid to the Fund will mean less cash available for the employer to spend on the provision of services. For instance:

- Higher pension Fund contributions may result in reduced council spending, which in turn could affect the resources available for council services, and/or greater pressure on council tax levels;
- Contributions which Academies pay to the Fund will therefore not be available to pay for providing education;
- Other employers will provide various services to the local community, perhaps through housing associations, charitable work, or contracting council services. If they are required to pay more in pension contributions to the LGPS then this may affect their ability to provide the local services.

Whilst all this is true, it should also be borne in mind that:

- The Fund provides invaluable financial security to local families, whether to those who formerly worked in the service of the local community who have now retired, or to their families after their death;
- The Fund must have the assets available to meet these retirement and death benefits, which in turn means that the various employers must each pay their own way. Lower contributions today will mean higher contributions tomorrow: deferring payments does not alter the employer's ultimate obligation to the Fund in respect of its current and former employees;
- Each employer will generally only pay for its own employees and ex-employees (and their dependants), not for those of other employers in the Fund;
- The Fund strives to maintain reasonably stable employer contribution rates where appropriate and possible;
- The Fund wishes to avoid the situation where an employer falls so far behind in managing its funding shortfall that its deficit becomes unmanageable in practice: such a situation may lead to employer insolvency and the resulting deficit falling on the other Fund employers. In that situation, those employers' services would in turn suffer as a result;
- Council contributions to the Fund should be at a suitable level, to protect the interests of different generations of council tax payers. For instance, underpayment of contributions for some years will need to be balanced by overpayment in other years; the council will wish to minimise the extent to which council tax payers in one period are in effect benefitting at the expense of those paying in a different period.

Overall, therefore, there is clearly a balance to be struck between the Fund's need for maintaining prudent funding levels, and the employers' need to allocate their resources appropriately. The Fund achieves this through various techniques which affect contribution increases to various degrees (see 3.1).

For instance, where an employer is considered relatively low risk then the Fund will permit greater smoothing (such as stabilisation or a longer deficit recovery period relative to other employers) which will temporarily produce lower contribution levels than would otherwise have applied. This is permitted in the expectation that the employer will still be able to meet its obligations for many years to come.

On the other hand, an employer whose risk assessment indicates a less strong covenant will generally be required to pay higher contributions (for instance, with a more prudent funding basis or a shorter deficit recovery period relative to other employers). This is because of the higher probability that at some point it will fail or be unable to meet its pension contributions, with its deficit in the Fund then falling to other Fund employers.

The Fund actively seeks employer input, including to its funding arrangements, through various means: see Appendix A.

3 Calculating contributions for individual Employers

3.1 General comments

A key challenge for the Administering Authority is to balance the need for stable, affordable employer contributions with the requirement to take a prudent, longer-term view of funding and ensure the solvency of the Fund. With this in mind, there are a number of methods which the Administering Authority may permit, in order to improve the stability of employer contributions. These include, where circumstances permit:-

- capping of employer contribution rate changes within a pre-determined range (“stabilisation”)
- the use of extended deficit recovery periods
- the phasing in of contribution rises or reductions
- the pooling of contributions amongst employers with similar characteristics
- the use of some form of security or guarantee to justify a lower contribution rate than would otherwise be the case.

These and associated issues are covered in this Section.

The Administering Authority recognises that there may occasionally be particular circumstances affecting individual employers that are not easily managed within the rules and policies set out in the Funding Strategy Statement. Therefore the Administering Authority may, at its sole discretion, direct the actuary to adopt alternative funding approaches on a case by case basis for specific employers.

3.2 The effect of paying contributions below the theoretical level

Employers which are permitted to use one or more of the above methods will often be paying, for a time, contributions less than the theoretical contribution rate. Such employers should appreciate that:

- their true long term liability (i.e. the actual eventual cost of benefits payable to their employees and ex-employees) is not affected by the choice of method,
- lower contributions in the short term will be assumed to incur a greater loss of investment returns on the deficit. Thus, deferring a certain amount of contribution will lead to higher contributions in the long-term, and
- it will take longer to reach full funding, all other things being equal.

Overleaf (3.3) is a summary of how the main funding policies differ for different types of employer, followed by more detailed notes where necessary.

Section 3.4 onwards deals with various other funding issues which apply to all employers.

3.3 The different approaches used for different employers

Type of employer	Scheduled Bodies			Community Admission Bodies and Designating Employers		Transferee Admission Bodies
Sub-type	**Local Authorities and Police (Tier 1)**	**Colleges,other FE establishments and Probation (Tier 2)**	**Academies (Tier 2)**	**Open to new entrants**	**Closed to new entrants**	**(all)**
Basis used	Ongoing, assumes long-term Fund participation (see Appendix E)			Ongoing, but may move to "gilts basis" - see Note (a)		Ongoing, assumes fixed contract term in the Fund (see Appendix E)
Future service rate	Projected Unit Credit approach (see Appendix D – D.2)				Attained Age approach (see Appendix D – D.2)	Projected Unit Credit approach if open, Attained Age approach otherwise (see Appendix D – D.2)
Stabilised rate?	Yes - see Note (b)	Yes - see Note (b)	Yes - see Note (b)	No	No	No
Maximum deficit recovery period – Note (c)	20 years	15 years	15 years	15 years	Future Working Lifetime, subject to 15 years maximum	Outstanding contract term
Deficit recovery payments – Note (d)	Monetary	Monetary	Monetary	Monetary	Monetary	Monetary
Treatment of surplus	Covered by stabilisation arrangement	Covered by stabilisation arrangement	Covered by stabilisation arrangement	Preferred approach: contributions kept at future service rate unless fully funded on a gilts basis.		Reduce contributions by spreading the surplus over the remaining contract term where appropriate.
Phasing of contribution changes	Covered by stabilisation arrangement	Covered by stabilisation arrangement	Covered by stabilisation arrangement	3 years - Note (e)	None	None
Review of rates – Note (f)	Administering Authority reserves the right to review contribution rates and amounts, and the level of security provided, at regular intervals between valuations					Particularly reviewed in last 3 years of contract
New employer	n/a	n/a	Note (g)	Note (h)		Notes (h) & (i)
Cessation of participation: cessation debt payable	Cessation is assumed not to be generally possible, as Scheduled Bodies are legally obliged to participate in the LGPS. In the rare event of cessation occurring (machinery of Government changes for example), the cessation debt principles applied would be as per Note (j).			Can be ceased subject to terms of admission agreement. Cessation debt will be calculated on a basis appropriate to the circumstances of cessation – see Note (j).		Participation is assumed to expire at the end of the contract. Cessation debt (if any) calculated on ongoing basis. Awarding Authority will be liable for future deficits and contributions arising.

Note (a) (Basis for CABs and Designating Employers closed to new entrants)

In the circumstances where:

- the employer is a Designating Employer, or an Admission Body but not a Transferee Admission Body, and
- the employer has no guarantor, and
- the admission agreement is likely to terminate, or the employer is likely to lose its last active member, within a timeframe considered appropriate by the Administering Authority to prompt a change in funding,

the Administering Authority may vary the discount rate used to set employer contribution rate. In particular contributions may be set for an employer to achieve full funding on a more prudent basis (e.g. using a discount rate set equal to gilt yields) by the time the agreement terminates or the last active member leaves, in order to protect other employers in the Fund. This policy will increase regular contributions and reduce, but not entirely eliminate, the possibility of a final deficit payment being required from the employer when a cessation valuation is carried out.

The Administering Authority also reserves the right to adopt the above approach in respect of those Designating Employers and Admission Bodies with no guarantor, where the strength of covenant is considered to be weak but there is no immediate expectation that the admission agreement will cease or the Designating Employer alters its designation.

Note (b) (Stabilisation)

Stabilisation is a mechanism where employer contribution rate variations from year to year are kept within a pre-determined range, thus allowing those employers' rates to be relatively stable. In the interests of stability and affordability of employer contributions, the Administering Authority, on the advice of the Fund Actuary, believes that stabilising contributions can still be viewed as a prudent longer-term approach. However, employers whose contribution rates have been "stabilised" (and may therefore be paying less than their theoretical contribution rate) should be aware of the risks of this approach and should consider making additional payments to the Fund if possible.

This stabilisation mechanism allows short term investment market volatility to be managed so as not to cause volatility in employer contribution rates, on the basis that a long term view can be taken on net cash inflow, investment returns and strength of employer covenant.

The current stabilisation mechanism applies if:

- the employer satisfies the eligibility criteria set by the Administering Authority (see below) and;
- there are no material events which cause the employer to become ineligible, e.g. significant reductions in active membership (due to outsourcing or redundancies), or changes in the nature of the employer (perhaps due to Government restructuring).

On the basis of extensive modelling carried out for the 2013 valuation exercise (see Section 4), the stabilised details are as follows:

Type of employer	"Standard" Council (Tier 1)	"Mature" Council (Tier 1)	Colleges and other Education establishments including Academies (Tier 2)
Max contribution increase	+0.5% of pay	+0.5% of pay	+1%
Max contribution decrease	-0.5% of pay	+0.5% of pay	-0.5%

The stabilisation criteria and limits will be reviewed at the 31 March 2016 valuation, to take effect from 1 April 2017. This will take into account the employer's membership profiles, the issues surrounding employer security, and other relevant factors.

Note (c) (Deficit Recovery Periods)

The deficit recovery period starts at the commencement of the revised contribution rate (1 April 2014 for the 2013 valuation). The Administering Authority would normally expect the same period to be used at successive triennial valuations, but would reserve the right to propose alternative spreading periods, for example where there were no new entrants.

Where stabilisation applies, the resulting employer contribution rate would be amended to comply with the stabilisation mechanism.

Note (d) (Deficit Recovery Payments)

The deficit recovery payments for each employer covering the three year period until the next valuation will usually be set monetary amounts.

Note (e) (Phasing in of contribution changes)

All phasing is subject to the Administering Authority being satisfied as to the strength of the employer's covenant.

Employers which have no active members or closed to new entrants at this valuation will not be phased.

Note (f) (Regular Reviews)

Such reviews may be triggered by significant events including but not limited to: significant reductions in payroll, altered employer circumstances, Government restructuring affecting the employer's business, or failure to pay contributions or arrange appropriate security as required by the Administering Authority.

The result of a review may be to require increased contributions (by strengthening the actuarial assumptions adopted, changing stabilisation parameters and/or moving to monetary levels of deficit recovery contributions), and/or an increased level of security or guarantee.

Note (g) (New Academy employers)

At the time of writing, the Fund's policies on academies' funding issues are as follows:

a) The new academy will be regarded as a separate employer in its own right and will not be pooled with other employers in the Fund. The only exception is where the academy is part of a Multi Academy Trust (MAT) in which case the academy's figures will be calculated as below but can be combined with those of the other academies in the MAT;

b) The new academy's past service liabilities on conversion will be calculated based on its active Fund members on the day before conversion. For the avoidance of doubt, these liabilities will include all past service of those members, but will exclude the liabilities relating to any former employees of the school who have deferred or pensioner status;

c) The new academy will be allocated an initial asset share from the ceding employer's assets in the Fund. This asset share will be calculated using the estimated funding position of the ceding employer at the date of academy conversion. The share will be based on the active members' funding level, having first allocated assets in the employer's share to fully fund deferred and pensioner members. The asset allocation will be based on market conditions and the academy's active Fund membership on the day prior to conversion;

d) The new academy's initial contribution rate will be calculated using market conditions, the ceding employer's funding position and, membership data, all as at the day prior to conversion;

e) As an alternative to (d), the academy will have the option to elect to pay contributions up to the next formal valuation in line with the ceding LEA instead. However, this election will not alter its asset or liability allocation as per (b) and (c) above. Ultimately, all academies remain responsible for their own allocated deficit. The Fund assumes that new academies will adopt this approach unless it is informed otherwise.

The Fund's policies on academies are subject to change in the light of any amendments to DCLG guidance. Any changes will be notified to academies, and will be reflected in a subsequent version of this FSS. In particular, policies (d) and (e) above will be reconsidered at each valuation.

Note (h) (New Admission Bodies)

With effect from 1 October 2012, the LGPS 2012 Miscellaneous Regulations introduced mandatory new requirements for all Admission Bodies brought into the Fund from that date. Under these Regulations, all new Admission Bodies will be required to provide some form of security, such as a guarantee from the letting employer, an indemnity or a bond. The security is required to cover some or all of the following:

- the strain cost of any redundancy early retirements resulting from the premature termination of the contract;
- allowance for the risk of asset underperformance;
- allowance for the risk of a fall in gilt yields;
- allowance for the possible non-payment of employer and member contributions to the Fund;
- the current deficit.

For all new Transferee Admission Bodies, the security must be to the satisfaction of the Administering Authority as well as the letting employer, and will be reassessed on an annual basis.

The Administering Authority will only consider requests from Community Admission Bodies (or other similar bodies, such as section 75 NHS partnerships) to join the Fund if they are sponsored by a Scheduled Body with tax raising powers, guaranteeing their liabilities and also providing a form of security as above.

The above approaches reduce the risk to other employers in the Fund, of potentially having to pick up any shortfall in respect of Admission Bodies ceasing with an unpaid deficit.

Note (i) (New Transferee Admission Bodies)

A new TAB usually joins the Fund as a result of the letting/outsourcing of some services from an existing employer (normally a Scheduled Body such as a council or academy) to another organisation (a “contractor”). This involves the TUPE transfer of some staff from the letting employer to the contractor. Consequently, for the duration of the contract, the contractor is a new participating employer in the Fund so that the transferring employees maintain their eligibility for LGPS membership. At the end of the contract the employees revert to the letting employer or to a replacement contractor.

Ordinarily, the TAB would be set up in the Fund as a new employer with responsibility for all the accrued benefits of the transferring employees; in this case, the contractor would usually be assigned an initial asset allocation equal to the past service liability value of the employees’ Fund benefits. The quid pro quo is that the contractor is then expected to ensure that its share of the Fund is also fully funded at the end of the contract: see Note (j).

Employers which “outsource” have flexibility in the way that they can deal with the pension risk potentially taken on by the contractor. Any approach taken here is at the discretion and risk of the outsourcing employer. Clearly as the risk ultimately resides with the employer letting the contract, it is for them to agree the appropriate route with the contractor:

- The Administering Authority should be informed if any risk sharing or retention agreement is entered into. Any risk sharing agreements should be detailed in a formal legal agreement. It may be the case that this details what the contractor is and isn’t responsible for, however, note all parties should take their own professional advice.

These agreements are generally out with the employers relationship with the Fund.

Note (j) (Admission Bodies Ceasing)

Notwithstanding the provisions of the Admission Agreement, the Administering Authority may consider any of the following as triggers for the cessation of an admission agreement with any type of body:

- Last active member ceasing participation in the Fund;
- The insolvency, winding up or liquidation of the Admission Body;
- Any breach by the Admission Body of any of its obligations under the Agreement that they have failed to remedy to the satisfaction of the Fund;
- A failure by the Admission Body to pay any sums due to the Fund within the period required by the Fund; or
- The failure by the Admission Body to renew or adjust the level of the bond or indemnity, or to confirm an appropriate alternative guarantor, as required by the Fund.

On cessation, the Administering Authority will instruct the Fund actuary to carry out a cessation valuation to determine whether there is any deficit or surplus. Where there is a deficit, payment of this amount in full would normally be sought from the Admission Body; where there is a surplus it should be noted that current legislation does not permit a refund payment to the Admission Body.

For non-Transferee Admission Bodies whose participation is voluntarily ended either by themselves or the Fund, or where a cessation event has been triggered, the Administering Authority must look to protect the interests of other ongoing employers. The actuary will therefore adopt an approach which, to the extent reasonably practicable, protects the other employers from the likelihood of any material loss emerging in future:

a) Where there is a guarantor for future deficits and contributions, the cessation valuation will normally be calculated using the ongoing basis as described in Appendix E;

b) Alternatively, it may be possible to simply transfer the former Admission Body's liabilities and assets to the guarantor, without needing to crystallise any deficit. This approach may be adopted where the employer cannot pay the contributions due, and this is within the terms of the guarantee. This can only be undertaken with the agreement of the guarantor and may impact on the guarantor's contribution rate.

c) Where a guarantor does not exist then, in order to protect other employers in the Fund, the cessation liabilities and final deficit will normally be calculated using a "gilts cessation basis", which is more prudent than the ongoing basis. This has no allowance for potential future investment outperformance above gilt yields, and has added allowance for future improvements in life expectancy. This could give rise to significant cessation debts being required.

Under (a) and (c), any shortfall would usually be levied on the departing Admission Body as a single lump sum payment. If this is not possible then the Fund would look to any bond, indemnity or guarantee in place for the employer.

In the event that the Fund is not able to recover the required payment in full, then the unpaid amounts fall to be shared amongst all of the other employers in the Fund. This may require an immediate revision to the Rates and Adjustments Certificate affecting other employers in the Fund, or instead be reflected in the contribution rates set at the next formal valuation following the cessation date

As an alternative, where the ceasing Admission Body is continuing in business, the Fund at its absolute discretion reserves the right to enter into an agreement with the ceasing Admission Body in relation to payments that may be due. Such agreements will make consideration of any additional security or indemnity that may be provided by the ceasing employer. The Fund reserves the right to seek immediate payment of any funding shortfall identified. The Administering Authority may need to seek legal advice in such cases, as the Body would have no contributing members.

3.4 Pooled contributions

From time to time the Administering Authority may set up pools for employers with similar characteristics. This will always be in line with its broader funding strategy.

With the advice of the Actuary the Administering Authority allows smaller employers of similar types to pool their contributions as a way of sharing experience and smoothing out the effects of costly but relatively rare events such as ill-health retirements or deaths in service.

Community Admission Bodies that are deemed by the Administering Authority to have closed to new entrants are not usually permitted to participate in a pool. Transferee Admission Bodies are usually also ineligible for pooling.

Smaller admitted bodies may be pooled with the letting employer, provided all parties (particularly the letting employer) agree.

Those employers which have been pooled are identified in the Rates and Adjustments Certificate.

3.5 Additional flexibility in return for added security

The Administering Authority may permit greater flexibility to the employer's contributions if the employer provides added security to the satisfaction of the Administering Authority.

Such flexibility includes a reduced rate of contribution, an extended deficit recovery period, or permission to join a pool with another body (e.g. the Local Authority).

Such security may include, but is not limited to, a suitable bond, a legally-binding guarantee from an appropriate third party, or security over an employer asset of sufficient value.

The degree of flexibility given may take into account factors such as:

- the extent of the employer's deficit;
- the amount and quality of the security offered;
- the employer's financial security and business plan;
- whether the admission agreement is likely to be open or closed to new entrants.

3.6 Non ill health early retirement costs

It is assumed that members' benefits are payable from the earliest age that the employee could retire without incurring a reduction to their benefit (and without requiring their employer's consent to retire). (**NB** the relevant age may be different for different periods of service, following the benefit changes from April 2008 and April 2014).
Employers are required to pay additional contributions ('strain') wherever an employee retires before attaining this age. The actuary's funding basis makes no allowance for premature retirement except on grounds of ill-health.

At the discretion of the Administering Authority the payment can be spread over a period up to 3 years (but no more than the outstanding contract term for a Transferee Admission Body):

3.7 Ill health early retirement costs

Admitted Bodies will usually have an ‘ill health allowance’; Scheduled Bodies may have this also, depending on their agreement terms with the Administering Authority. The Fund monitors each employer’s ill health experience on an ongoing basis. If the cumulative cost of ill health retirement in any financial year exceeds the allowance at the previous valuation, the employer will be charged additional contributions on the same basis as apply for non ill-health cases. Details will be included in each separate Admission Agreement.

3.8 Employers with no remaining active members

In general an employer ceasing in the Fund, due to the departure of the last active member, will pay a cessation debt on an appropriate basis (see 3.3, Note (j)) and consequently have no further obligation to the Fund. Thereafter it is expected that one of two situations will eventually arise:

a) The employer’s asset share runs out before all its ex-employees’ benefits have been paid. In this situation the other Fund employers will be required to contribute to pay all remaining benefits: this will be done by the Fund actuary apportioning the remaining liabilities on a pro-rata basis at successive formal valuations;

b) The last ex-employee or dependant dies before the employer’s asset share has been fully utilised. In this situation the remaining assets would be apportioned pro-rata by the Fund’s actuary to the other Fund

c) In exceptional circumstances the Fund may permit an employer with no remaining active members to continue contributing to the Fund. This would require the provision of a suitable security or guarantee, as well as a written ongoing commitment to fund the remainder of the employer’s obligations over an appropriate period. The Fund would reserve the right to invoke the cessation requirements in the future, however. The Administering Authority may need to seek legal advice in such cases, as the employer would have no contributing members.

3.9 Policies on bulk transfers

Each case will be treated on its own merits, but in general:

- The Fund will not pay bulk transfers greater than the lesser of (a) the asset share of the transferring employer in the Fund, and (b) the value of the past service liabilities of the transferring members;
- The Fund will not grant added benefits to members bringing in entitlements from another Fund unless the asset transfer is sufficient to meet the added liabilities;
- The Fund may permit shortfalls to arise on bulk transfers if the Fund employer has suitable strength of covenant and commits to meeting that shortfall in an appropriate period. This may require the employer’s Fund contributions to increase between valuations.

4 Funding strategy and links to investment strategy

4.1 What is the Fund's investment strategy?

The Fund has built up assets over the years, and continues to receive contribution and other income. All of this must be invested in a suitable manner, which is the investment strategy.

Investment strategy is set by the administering authority after taking independent advice. The precise mix, manager make up and target returns are set out in the Statement of Investment Principles (SIP), which is available to members and employers.

The investment strategy is set for the long-term, but is reviewed from time to time. Normally a full review is carried out after each actuarial valuation, and is kept under review between actuarial valuations to ensure that it remains appropriate to the Fund's liability profile.

The same investment strategy is currently followed for all employers.

4.2 What is the link between funding strategy and investment strategy?

The Fund must be able to meet all benefit payments as and when they fall due. These payments will be met by contributions (resulting from the funding strategy) or asset returns and income (resulting from the investment strategy). To the extent that investment returns or income fall short, then higher cash contributions are required from employers, and vice versa

Therefore, the funding and investment strategies are inextricably linked.

4.3 How does the funding strategy reflect the Fund's investment strategy?

In the opinion of the Fund actuary, the current funding policy is consistent with the current investment strategy of the Fund. The asset outperformance assumption contained in the discount rate (see E3) is within a range that would be considered acceptable for funding purposes; it is also considered to be consistent with the requirement to take a "prudent longer-term view" of the funding of liabilities as required by the UK Government (see A1).

However, in the short term – such as the three yearly assessments at formal valuations – there is the scope for considerable volatility and there is a material chance that in the short-term and even medium term, asset returns will fall short of this target. The stability measures described in Section 3 will damp down, but not remove, the effect on employers' contributions.

The Fund does not hold a contingency reserve to protect it against the volatility of equity investments.

The Actuary has developed four key measures which capture the essence of the Fund's strategies, both funding and investment:

- Prudence - the Fund should have a reasonable expectation of being fully funded in the long term;
- Affordability – how much can employers afford;
- Stewardship – the assumptions used should be sustainable in the long term, without having to resort to overly optimistic assumptions about the future to maintain an apparently healthy funding position;
- Stability – employers should not see significant moves in their contribution rates from one year to the next, and this will help to provide a more stable budgeting environment.

The key problem is that the key objectives often conflict.

For example, minimising the long term cost of the scheme (i.e. keeping employer rates affordable) is best achieved by investing in higher returning assets e.g. equities. However, equities are also very volatile (i.e. go up and down fairly frequently in fairly large moves), which conflicts with the objective to have stable contribution rates.

Therefore a balance needs to be maintained between risk and reward, which has been considered by the use of Asset Liability Modelling: this is a set of calculation techniques applied by the Fund's actuary, to model the range of potential future solvency levels and contribution rates.

The Actuary was able to model the impact of these four key areas, for the purpose of setting a stabilisation approach (see 3.3 Note (b)). The modelling demonstrated that retaining the present investment strategy, coupled with constraining employer contribution rate changes as described in 3.3 Note (b), struck an appropriate balance between the above objectives. In particular the stabilisation approach currently adopted meets the need for stability of contributions without jeopardising the Administering Authority's aims of prudent stewardship of the Fund.

Whilst the current stabilisation mechanism is to remain in place until 2017, it should be noted that this will need to be reviewed at subsequent valuations.

Appendix A – Regulatory framework

A1 Why does the Fund need an FSS?

The Department for Communities and Local Government (DCLG) has stated that the purpose of the FSS is:

- *"to establish a **clear and transparent fund-specific strategy** which will identify how employers' pension liabilities are best met going forward;*
- *to support the regulatory framework to maintain **as nearly constant employer contribution rates as possible**; and*
- *to take a **prudent longer-term view** of funding those liabilities."*

These objectives are desirable individually, but may be mutually conflicting.

The requirement to maintain and publish a FSS is contained in LGPS Regulations which are updated from time to time. In publishing the FSS the Administering Authority has to have regard to any guidance published by Chartered Institute of Public Finance and Accountancy (CIPFA) (most recently in 2012) and to its Statement of Investment Principles.

This is the framework within which the Fund's actuary carries out triennial valuations to set employers' contributions and provides recommendations to the Administering Authority when other funding decisions are required, such as when employers join or leave the Fund. The FSS applies to all employers participating in the Fund.

A2 Does the Administering Authority consult anyone on the FSS?

Yes. This is required by LGPS Regulations. It is covered in more detail by the most recent CIPFA guidance, which states that the FSS must first be subject to "consultation with such persons as the authority considers appropriate", and should include "a meaningful dialogue at officer and elected member level with council tax raising authorities and with corresponding representatives of other participating employers".

In practice, for the Fund, the consultation process for this FSS was as follows:

a) A draft version of the FSS was issued to all participating employers in [DATE] for comment;

b) Comments were requested within 21] days;

c) Following the end of the consultation period the FSS was updated where required and then published, in [DATE].

A3 How is the FSS published?

The FSS is made available through the following routes:

- Published on the website, at www.norfolkpensionfund.org;

A4 How often is the FSS reviewed?

The FSS is reviewed in detail at least every three years as part of the triennial valuation. This version is expected to remain unaltered until it is consulted upon as part of the formal process for the next valuation in 2016.

It is possible that (usually slight) amendments may be needed within the three year period.

These would be needed to reflect any regulatory changes, or alterations to the way the Fund operates (e.g. to accommodate a new class of employer).
Any such amendments would be consulted upon as appropriate:

- trivial amendments would be simply notified at the next round of employer communications,
- amendments affecting only one class of employer would be consulted with those employers,
- other more significant amendments would be subject to full consultation.

In any event, changes to the FSS would need agreement by the Pensions Committee and would be included in the relevant Committee Meeting minutes.

A5 How does the FSS fit into other Fund documents?

The FSS is a summary of the Fund's approach to funding liabilities. It is not an exhaustive statement of policy on all issues, for example there are a number of separate statements published by the Fund including the Statement of Investment Principles, Governance Strategy and Communications Strategy. In addition, the Fund publishes an Annual Report and Accounts with up to date information on the Fund.

These documents can be found on the web at www.norfolkpensionfund.org.

Appendix B – Responsibilities of key parties

The efficient and effective operation of the Fund needs various parties to each play their part.

B1 The Administering Authority should:-

- operate the Fund as per the LGPS Regulations;
- effectively manage any potential conflicts of interest arising from its dual role as Administering Authority and a Fund employer;
- collect employer and employee contributions, and investment income and other amounts due to the Fund;
- ensure that cash is available to meet benefit payments as and when they fall due;
- pay from the Fund the relevant benefits and entitlements that are due;
- invest surplus monies (i.e. contributions and other income which are not immediately needed to pay benefits) in accordance with the Fund's Statement of Investment Principles (SIP) and LGPS Regulations;
- communicate appropriately with employers so that they fully understand their obligations to the Fund;
- take appropriate measures to safeguard the Fund against the consequences of employer default;
- manage the valuation process in consultation with the Fund's actuary;
- prepare and maintain a FSS and a SIP, after consultation;
- notify the Fund's actuary of material changes which could affect funding (this is covered in a separate agreement with the actuary); and
- monitor all aspects of the fund's performance and funding and amend the FSS/SIP as necessary and appropriate.

B2 The Individual Employer should:-

- deduct contributions from employees' pay correctly;
- pay all contributions, including their own as determined by the actuary, promptly by the due date;
- have a policy and exercise discretions within the regulatory framework;
- make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of scheme benefits, early retirement strain; and
- notify the Administering Authority promptly of all changes to its circumstances, prospects or membership, which could affect future funding.

B3 The Fund Actuary should:-

- prepare valuations, including the setting of employers' contribution rates. This will involve agreeing assumptions with the Administering Authority, having regard to the FSS and LGPS Regulations, and targeting each employer's solvency appropriately;
- provide advice relating to new employers in the Fund, including the level and type of bonds or other forms of security (and the monitoring of these);
- prepare advice and calculations in connection with bulk transfers and individual benefit-related matters;
- assist the Administering Authority in considering possible changes to employer contributions between formal valuations, where circumstances suggest this may be necessary;

- advise on the termination of Admission Bodies' participation in the Fund; and
- fully reflect actuarial professional guidance and requirements in the advice given to the Administering Authority.

B4 Other parties:-

- investment advisers (either internal or external) should ensure the Fund's SIP remains appropriate, and consistent with this FSS;
- investment managers, custodians and bankers should all play their part in the effective investment (and dis-investment) of Fund assets, in line with the SIP;
- auditors should comply with their auditing standards, ensure Fund compliance with all requirements, monitor and advise on fraud detection, and sign off annual reports and financial statements as required;
- governance advisers may be appointed to advise the Administering Authority on efficient processes and working methods in managing the Fund;
- legal advisers (either internal or external) should ensure the Fund's operation and management remains fully compliant with all regulations and broader local government requirements, including the Administering Authority's own procedures.

Appendix C – Key risks and controls

C1 Types of risk

The Administering Authority has an active risk management programme in place. The measures that it has in place to control key risks are summarised below under the following headings:

- financial;
- demographic;
- regulatory; and
- governance.

C2 Financial risks

Risk	Summary of Control Mechanisms
Fund assets fail to deliver returns in line with the anticipated returns underpinning valuation of liabilities over the long-term.	Only anticipate long-term return on a relatively prudent basis to reduce risk of under-performing. Assets invested on the basis of specialist advice, in a suitably diversified manner across asset classes, geographies, managers, etc. Analyse progress at three yearly valuations for all employers. Inter-valuation roll-forward of liabilities between valuations at whole Fund level.
Inappropriate long-term investment strategy.	Overall investment strategy options considered as an integral part of the funding strategy. Used asset liability modelling to measure 4 key outcomes. Chosen option considered to provide the best balance.
Fall in risk-free returns on Government bonds, leading to rise in value placed on liabilities.	Stabilisation modelling at whole Fund level allows for the probability of this within a longer term context. Inter-valuation monitoring, as above. Some investment in bonds helps to mitigate this risk.
Active investment manager under-performance relative to benchmark.	Quarterly investment monitoring analyses market performance and active managers relative to their index benchmark.
Pay and price inflation significantly more than anticipated.	The focus of the actuarial valuation process is on real returns on assets, net of price and pay increases. Inter-valuation monitoring, as above, gives early warning.

Risk	Summary of Control Mechanisms
	Some investment in bonds also helps to mitigate this risk. Employers pay for their own salary awards and should be mindful of the geared effect on pension liabilities of any bias in pensionable pay rises towards longer-serving employees. Annual pay increase monitoring at employer level will identify pay award strains which can then be immediately recharged to employers.
Effect of possible increase in employer's contribution rate on service delivery and admission/scheduled bodies	An explicit stabilisation mechanism has been agreed as part of the funding strategy. Other measures are also in place to limit sudden increases in contributions.
Orphaned employers give rise to added costs for the Fund	The Fund seeks a cessation debt (or security/guarantor) to minimise the risk of this happening in the future. If it occurs, the Actuary calculates the added cost spread pro-rata among all employers – (see 3.9).

C3 Demographic risks

Risk	Summary of Control Mechanisms
Pensioners living longer, thus increasing cost to Fund.	Set mortality assumptions with some allowance for future increases in life expectancy. The Fund Actuary has direct access to the experience of over 50 LGPS funds which allows early identification of changes in life expectancy that might in turn affect the assumptions underpinning the valuation.
Maturing Fund – i.e. proportion of actively contributing employees declines relative to retired employees.	Continue to monitor at each valuation, seek monetary amounts rather than percentage of pay and consider alternative investment strategies if deemed appropriate.
Deteriorating patterns of early retirements	Employers are charged the extra cost of non ill-health retirements following each individual decision. Employer ill health retirement experience is monitored, and insurance is an option the Fund will consider supporting.
Reductions in payroll causing insufficient deficit	In many cases this may not be sufficient cause for concern, and will in effect be caught at the next formal

Risk	Summary of Control Mechanisms
recovery payments	valuation. However, there are protections where there is concern, as follows: Employers in the stabilisation mechanism may be brought out of that mechanism to permit appropriate contribution increases (see Note (b) to 3.3). For other employers, review of contributions is permitted in general between valuations (see Note (f) to 3.3) and may require a move in deficit contributions from a percentage of payroll to fixed monetary amounts.

C4 Regulatory risks

Risk	Summary of Control Mechanisms
Changes to national pension requirements and/or HMRC rules e.g. changes arising from public sector pensions reform.	The Administering Authority considers all consultation papers issued by the Government and comments where appropriate. The results of the most recent reforms have been built into the 2013 valuation. Any changes to member contribution rates or benefit levels will be carefully communicated with members to minimise possible opt-outs or adverse actions.

C5 Governance risks

Risk	Summary of Control Mechanisms
Administering Authority unaware of structural changes in an employer's membership (e.g. large fall in employee members, large number of retirements) or not advised of an employer closing to new entrants.	The Administering Authority has a close relationship with employing bodies and communicates required standards e.g. for submission of data. The Actuary may revise the rates and Adjustments certificate to increase an employer's contributions (under Regulation 38) between triennial valuations Deficit contributions generally expressed as monetary amounts.
Actuarial or investment advice is not sought, or is not heeded, or proves to be insufficient in some way	The Administering Authority maintains close contact with its specialist advisers. Advice is delivered via formal meetings involving

Risk	Summary of Control Mechanisms
	Elected Members, and recorded appropriately. Actuarial advice is subject to professional requirements such as peer review.
Administering Authority failing to commission the Fund Actuary to carry out a termination valuation for a departing Admission Body.	The Administering Authority requires employers with Best Value contractors to inform it of forthcoming changes. Community Admission Bodies' memberships are monitored and, if active membership decreases, steps will be taken.
An employer ceasing to exist with insufficient funding or adequacy of a bond.	The Administering Authority believes that it would normally be too late to address the position if it was left to the time of departure. The risk is mitigated by: Seeking a funding guarantee from another scheme employer, or external body, where-ever possible (see Notes (h) and (j) to 3.3). Alerting the prospective employer to its obligations and encouraging it to take independent actuarial advice. Vetting prospective employers before admission. Where permitted under the regulations requiring a bond is considered. Requiring new Community Admission Bodies to have a guarantor. Reviewing contributions well ahead of cessation if thought appropriate (see Note (a) to 3.3).

Appendix D – The calculation of Employer contributions

In Section 2 there was a broad description of the way in which contribution rates are calculated. This Appendix considers these calculations in much more detail.

The calculations involve actuarial assumptions about future experience, and these are described in detail in Appendix E.

D1 What is the difference between calculations across the whole Fund and calculations for an individual employer?

Employer contributions are normally made up of two elements:

a) the estimated cost of future benefits being accrued, referred to as the "future service rate"; plus

b) an adjustment for the funding position of accrued benefits relative to the Fund's solvency target, "*past service adjustment*". If there is a surplus there may be a reduction in the employer's contribution rate. If there is a deficit there will be an increase in the employer's contribution rate, with the surplus or deficit spread over an appropriate period. The aim is to return the employer to full funding over that period. See Section 3 for deficit recovery periods.

The Fund's actuary is required by the regulations to report the *Common Contribution Rate*[1], for all employers collectively at each triennial valuation. It combines items (a) and (b) and is expressed as a percentage of pay; it is in effect an average rate across all employers in the Fund.

The Fund's actuary is also required to adjust the Common Contribution Rate for circumstances which are deemed "peculiar" to an individual employer[2]. It is the adjusted contribution rate which employers are actually required to pay. The sorts of "peculiar" factors which are considered are discussed below.

In effect, the *Common Contribution Rate* is a notional quantity. Separate future service rates are calculated for each employer together with individual past service adjustments according to employer-specific past service deficit spreading and increased employer contribution phasing periods.

D2 How is the Future Service Rate calculated?

The future service element of the employer contribution rate is calculated with the aim that these contributions will meet benefit payments in respect of members' **future** service in the Fund. This is based upon the cost (in excess of members' contributions) of the benefits which employee members earn from their service each year.

The future service rate is calculated separately for all the employers, although employers within a pool will pay the contribution rate applicable to the pool as a whole. The calculation is on the "ongoing" valuation basis (see Appendix E), but where it is considered appropriate to do so the Administering Authority reserves the right to set a future service rate by reference to liabilities valued on a more prudent basis (see Section 3).

The approach used to calculate each employer's future service contribution rate depends on whether or not new entrants are being admitted. Employers should note that it is only Admission Bodies and Designating Employers that may have the power not to automatically admit all eligible new staff to the Fund, depending on the terms of their Admission Agreements and employment contracts.

[1] See LGPS (Administration) Regulations 36(5).
[2] See LGPS (Administration) Regulations 36(7).

a) Employers which admit new entrants

These rates will be derived using the “Projected Unit Method” of valuation with a one year period, i.e. only considering the cost of the next year’s benefit accrual and contribution income. If future experience is in line with assumptions, and the employer’s membership profile remains stable, this rate should be broadly stable over time. If the membership of employees matures (e.g. because of lower recruitment) the rate would rise over time.

b) Employers which do not admit new entrants

To give more long term stability to such employers’ contributions, the “Attained Age” funding method is normally adopted. This measures benefit accrual and contribution income over the whole future anticipated working lifetimes of current active employee members.

Both approaches include expenses of administration to the extent that they are borne by the Fund, and include allowances for benefits payable on death in service and ill health retirement.

D3 How is the Solvency / Funding Level calculated?

The Fund’s actuary is required to report on the “solvency” of the whole Fund in a valuation which should be carried out at least once every three years. As part of this valuation, the actuary will calculate the solvency position of each employer.

‘Solvency” is defined to be the ratio of the market value of the employer’s asset share to the value placed on accrued benefits on the Fund actuary’s chosen assumptions. This quantity is known as a funding level.

For the value of the employer’s asset share, see D5 below.

For the value of benefits, the Fund actuary agrees the assumptions to be used with the Administering Authority – see Appendix E. These assumptions are used to calculate the present value of all benefit payments expected in the future, relating to that employer’s current and former employees, based on pensionable service to the valuation date only (i.e. ignoring further benefits to be built up in the future).

The Fund operates the same target funding level for all employers of 100% of its accrued liabilities valued on the ongoing basis, unless otherwise determined (see Section 3).

D4 What affects a given employer’s valuation results?

The results of these calculations for a given individual employer will be affected by:

- past contributions relative to the cost of accruals of benefits;
- different liability profiles of employers (e.g. mix of members by age, gender, service vs. salary);
- the effect of any differences in the valuation basis on the value placed on the employer’s liabilities;
- any different deficit/surplus spreading periods or phasing of contribution changes;
- the difference between actual and assumed rises in pensionable pay;
- the difference between actual and assumed increases to pensions in payment and deferred pensions;
- the difference between actual and assumed retirements on grounds of ill-health from active status;
- the difference between actual and assumed amounts of pension ceasing on death;
- the additional costs of any non ill-health retirements relative to any extra payments made;

over the period between each triennial valuation.

Actual investment returns achieved on the Fund between each valuation are applied proportionately across all employers, to the extent that employers in effect share the same investment strategy. Transfers of liabilities between employers within the Fund occur automatically within this process, with a sum broadly equivalent to the reserve required on the ongoing basis being exchanged between the two employers.

D5 How is each employer's asset share calculated?

The Administering Authority does not account for each employer's assets separately. Instead, the Fund's actuary is required to apportion the assets of the whole Fund between the employers, at each triennial valuation.

This apportionment uses the income and expenditure figures provided for certain cash flows for each employer. This process adjusts for transfers of liabilities between employers participating in the Fund, but does make a number of simplifying assumptions. The split is calculated using an actuarial technique known as "analysis of surplus".

The Fund actuary does not allow for certain relatively minor events, including but not limited to:

- the actual timing of employer contributions within any financial year;
- the effect of the premature payment of any deferred pensions on grounds of incapacity.

These effects are swept up within a miscellaneous item in the analysis of surplus, which is split between employers in proportion to their liabilities.

The methodology adopted means that there will inevitably be some difference between the asset shares calculated for individual employers and those that would have resulted had they participated in their own ring-fenced section of the Fund.

The asset apportionment is capable of verification but not to audit standard. The Administering Authority recognises the limitations in the process, but it considers that the Fund actuary's approach addresses the risks of employer cross-subsidisation to an acceptable degree.

Appendix E – Actuarial assumptions

E1 What are the actuarial assumptions?

These are expectations of future experience used to place a value on future benefit payments ("the liabilities"). Assumptions are made about the amount of benefit payable to members (the financial assumptions) and the likelihood or timing of payments (the demographic assumptions). For example, financial assumptions include investment returns, salary growth and pension increases; demographic assumptions include life expectancy, probabilities of ill-health early retirement, and proportions of member deaths giving rise to dependants' benefits.

Changes in assumptions will affect the measured value of future service accrual and past service liabilities, and hence the measured value of the past service deficit. However, different assumptions will not of course affect the actual benefits payable by the Fund in future.

The combination of all assumptions is described as the "basis". A more optimistic basis might involve higher assumed investment returns (discount rate), or lower assumed salary growth, pension increases or life expectancy; a more optimistic basis will give lower liability values and lower employer costs. A more prudent basis will give higher liability values and higher employer costs.

E2 What basis is used by the Fund?

The Fund's standard funding basis is described as the "ongoing basis", which applies to most employers in most circumstances. This is described in more detail below. It anticipates employers remaining in the Fund in the long term.

However, in certain circumstances, typically where the employer is not expected to remain in the Fund long term, a more prudent basis applies: see Note (a) to 3.3.

E3 What assumptions are made in the ongoing basis?

a) Investment return / discount rate

The key financial assumption is the anticipated return on the Fund's investments. This "discount rate" assumption makes allowance for an anticipated out-performance of Fund returns relative to long term yields on UK Government bonds ("gilts"). There is, however, no guarantee that Fund returns will out-perform gilts. The risk is greater when measured over short periods such as the three years between formal actuarial valuations, when the actual returns and assumed returns can deviate sharply.

Given the very long-term nature of the liabilities, a long term view of prospective asset returns is taken. The long term in this context would be 20 to 30 years or more.

For the purpose of the triennial funding valuation at 31 March 2013 and setting contribution rates effective from 1 April 2014, the Fund actuary has assumed that future investment returns earned by the Fund over the long term will be 1.55% per annum greater than gilt yields at the time of the valuation for the majority of employers (this is the same as that used at the 2010 valuation). In the opinion of the Fund actuary, based on the current investment strategy of the Fund, this asset out-performance assumption is within a range that would be considered acceptable for the purposes of the funding valuation.

b) Salary growth

Pay for public sector employees is currently subject to restriction by the UK Government until 2016. Although this "pay freeze" does not officially apply to local government and associated employers, it has been suggested that they are likely to show similar restraint in respect of pay awards. Based on long term historical analysis of the membership in LGPS funds, the salary increase assumption at the 2013 valuation has been set to equal the retail prices index (RPI) per annum. This is a change from the previous valuation, which assumed a three year restriction at 1% per annum followed by longer term growth at RPI plus 1.5% per annum.

The fund will monitor pay growth and put in place a recharge policy should there be a strain cost in respect of pay rises being higher than assumed.

c) Pension increases

Since 2011 the consumer prices index (CPI), rather than RPI, has been the basis for increases to public sector pensions in deferment and in payment. This change was allowed for in the valuation calculations as at 31 March 2010. Note that the basis of such increases is set by the Government, and is not under the control of the Fund or any employers.

As at the previous valuation, we derive our assumption for RPI from market data as the difference between the yield on long-dated fixed interest and index-linked government bonds. This is then reduced to arrive at the CPI assumption, to allow for the "formula effect" of the difference between RPI and CPI. At this valuation, we propose a reduction of 0.8% per annum. This is a larger reduction than at 2010, which will serve to reduce the value placed on the Fund's liabilities (all other things being equal).

d) Life expectancy

The demographic assumptions are intended to be best estimates of future experience in the Fund based on past experience of LGPS funds which participate in Club Vita, the longevity analytics service used by the Fund, and endorsed by the actuary.

The longevity assumptions that have been adopted at this valuation are a bespoke set of "VitaCurves", produced by the Club Vita's detailed analysis, which are specifically tailored to fit the membership profile of the Fund. These curves are based on the data provided by the Fund for the purposes of this valuation.

It is acknowledged that future life expectancy and, in particular, the allowance for future improvements in life expectancy, is uncertain. There is a consensus amongst actuaries, demographers and medical experts that life expectancy is likely to improve in the future. Allowance has been made in the ongoing valuation basis for future improvements in line with "medium cohort" and a 1.25% per annum minimum underpin to future reductions in mortality rates. This is a higher allowance for future improvements than was made in 2010.

The combined effect of the above changes from the 2010 valuation approach, is to add around a year of life expectancy on average. The approach taken is considered reasonable in light of the long term nature of the Fund and the assumed level of security underpinning members' benefits.

e) General

The same financial assumptions are adopted for all employers, in deriving the past service deficit and the future service rate: as described in (3.3), these calculated figures are translated in different ways into employer contributions, depending on the employer's circumstances.

The demographic assumptions, in particular the life expectancy assumption, in effect vary by type of member and so reflect the different membership profiles of employers.

Appendix F – Glossary

Actuarial assumptions/basis The combined set of assumptions made by the actuary, regarding the future, to calculate the value of **liabilities**. The main assumptions will relate to the **discount rate**, salary growth, pension increases and longevity. More prudent assumptions will give a higher liability value, whereas more optimistic assumptions will give a lower value.

Administering Authority The council with statutory responsibility for running the Fund, in effect the Fund's "trustees".

Admission Bodies Employers which voluntarily participate in the Fund, so that their employees and ex-employees are **members**. There will be an Admission Agreement setting out the employer's obligations. For more details (see 2.5).

Common contribution rate The Fund-wide **future service rate** plus **past service adjustment**. It should be noted that this will differ from the actual contributions payable by individual **employers**.

Covenant The assessed financial strength of the employer. A strong covenant indicates a greater ability (and willingness) to pay for pension obligations in the long run. A weaker covenant means that it appears that the employer may have difficulties meeting its pension obligations in full over the longer term.

Deficit The shortfall between the assets value and the **liabilities** value. This relates to assets and liabilities built up to date, and ignores the future build-up of pension (which in effect is assumed to be met by future contributions).

Deficit repair/recovery period The target length of time over which the current **deficit** is intended to be paid off. A shorter period will give rise to a higher annual **past service adjustment** (deficit repair contribution), and vice versa.

Designating Employer Employers such as town and parish councils that are able to participate in the LGPS via resolution. These employers can designate which of their employees are eligible to join the Fund.

Discount rate The annual rate at which future assumed cashflows (in and out of the Fund) are discounted to the present day. This is necessary to provide a **liabilities** value which is consistent with the present day value of the assets, to calculate the **deficit**. A lower discount rate gives a higher liabilities value, and vice versa. It is similarly used in the calculation of the **future service rate** and the **common contribution rate**.

Employer An individual participating body in the Fund, which employs (or used to employ) **members** of the Fund. Normally the assets and **liabilities** values for each employer are individually tracked, together with its **future service rate** at each **valuation**.

Funding level The ratio of assets value to **liabilities** value: for further details (see 2.2).

Future service rate	The actuarially calculated cost of each year's build-up of pension by the current active **members**, excluding members' contributions but including Fund administrative expenses. This is calculated using a chosen set of **actuarial assumptions**.
Gilt	A UK Government bond, ie a promise by the Government to pay interest and capital as per the terms of that particular gilt, in return for an initial payment of capital by the purchaser. Gilts can be "fixed interest", where the interest payments are level throughout the gilt's term, or "index-linked" where the interest payments vary each year in line with a specified index (usually RPI). Gilts can be bought as assets by the Fund, but their main use in funding is as an objective measure of solvency.
Guarantee / guarantor	A formal promise by a third party (the guarantor) that it will meet any pension obligations not met by a specified employer. The presence of a guarantor will mean, for instance, that the Fund can consider the employer's **covenant** to be as strong as its guarantor's.
Letting employer	An employer which outsources or transfers a part of its services and workforce to another employer (usually a contractor). The contractor will pay towards the LGPS benefits accrued by the transferring members, but ultimately the obligation to pay for these benefits will revert to the letting employer. A letting employer will usually be a local authority, but can sometimes be another type of employer such as an Academy.
Liabilities	The actuarially calculated present value of all pension entitlements of all **members** of the Fund, built up to date. This is compared with the present market value of Fund assets to derive the **deficit**. It is calculated on a chosen set of **actuarial assumptions**.
LGPS	The Local Government Pension Scheme, a public sector pension arrangement put in place via Government Regulations, for workers in local government. These Regulations also dictate eligibility (particularly for Scheduled Bodies), members' contribution rates, benefit calculations and certain governance requirements. The LGPS is divided into 101 Funds which map the UK. Each LGPS Fund is autonomous to the extent not dictated by Regulations, e.g. regarding investment strategy, employer contributions and choice of advisers.
Maturity	A general term to describe a Fund (or an employer's position within a Fund) where the members are closer to retirement (or more of them already retired) and the investment time horizon is shorter. This has implications for investment strategy and, consequently, funding strategy.
Members	The individuals who have built up (and may still be building up) entitlement in the Fund. They are divided into actives (current employee members), deferreds (ex-employees who have not yet retired) and pensioners (ex-employees who have now retired, and dependants of deceased ex-employees).
Past service adjustment	The part of the employer's annual contribution which relates to past service **deficit** repair.

Pooling	Employers may be grouped together for the purpose of calculating contribution rates, so that their combined membership and asset shares are used to calculate a single contribution rate applicable to all employers in the pool. A pool may still require each individual employer to ultimately pay for its own share of **deficit**, or (if formally agreed) it may allow **deficits** to be passed from one employer to another. For further details of the Fund's current pooling policy (see 3.4).
Profile	The profile of an employer's membership or liability reflects various measurements of that employer's **members**, ie current and former employees. This includes: the proportions which are active, deferred or pensioner; the average ages of each category; the varying salary or pension levels; the lengths of service of active members vs their salary levels, etc. A membership (or liability) profile might be measured for its **maturity** also.
Rates and Adjustments Certificate	A formal document required by the LGPS Regulations, which must be updated at least every three years at the conclusion of the formal **valuation**. This is completed by the actuary and confirms the contributions to be paid by each employer (or pool of employers) in the Fund for the three year period until the next valuation is completed.
Scheduled Bodies	Types of employer explicitly defined in the LGPS Regulations, whose employers must be offered membership of their local LGPS Fund. These include Councils, colleges, universities, academies, police and fire authorities etc, other than employees who have entitlement to a different public sector pension scheme (e.g. teachers, police and fire officers, university lecturers).
Solvency	In a funding context, this usually refers to a 100% **funding level**, ie where the assets value equals the **liabilities** value.
Stabilisation	Any method used to smooth out changes in employer contributions from one year to the next. This is very broadly required by the LGPS Regulations, but in practice is particularly employed for large stable employers in the Fund. Different methods may involve: probability-based modelling of future market movements; longer deficit recovery periods; higher discount rates; or some combination of these.
Theoretical contribution rate	The employer's contribution rate, including both **future service rate** and **past service adjustment**, which would be calculated on the standard **actuarial basis**, before any allowance for **stabilisation** or other agreed adjustment.
Valuation	An actuarial investigation to calculate the liabilities, future service contribution rate and common contribution rate for a Fund, and usually individual employers too. This is normally carried out in full every three years (last done as at 31 March 2013), but can be approximately updated at other times. The assets value is based on market values at the valuation date, and the liabilities value and contribution rates are based on long term bond market yields at that date also.

Appendix G - Salary growth: managing the risk

What is salary growth strain?

The Local Government Pension Scheme (LGPS) is a 'final salary' scheme so a member's pension is directly linked to their salary at retirement. This means that salary increases awarded to your employees have a direct impact on your total pension costs. At each triennial valuation of the pension fund, the actuary makes an assumption about the level of future salary growth. At the next valuation, the actuary then assesses the difference between the increases actually awarded over the last three years compared to those assumed. If salary increases were higher than anticipated then this will lead to higher pension costs. This increase in costs is referred to as 'salary growth strain'.

Why is the salary growth strain calculated?

At previous formal valuations, the actuary has assumed a level of future pay growth based on historic evidence which suggests pay rises are, on average, around 1.5% p.a. above inflation. At the 2013 valuation, the fund has discussed the appropriateness of such an assumption in light of recent economic conditions and the outlook for future long term pay awards. The actuary has agreed to use a much lower assumption at this valuation, equal to the rate of retail price inflation ("RPI"). A lower salary increase assumption benefits employers in that the value placed on their pension costs are reduced via an improved balance sheet position and lower calculated contribution rate (all else being equal). However, this places a greater risk on the fund of employers awarding larger than expected pay increases and not being able to meet the additional pension costs in the future. Therefore it is appropriate for the fund to put in place a mechanism that helps control this risk.

How will the mechanism work?

Salary increases will be monitored annually and any salary growth strain arising will be immediately billed to the responsible employer.

At each year end, the Fund will provide salary data for all your employees to the actuary who will calculate whether any salary growth strain has occurred over the year. The actuary will compare each member's salary at the year end (e.g. 31 March 2014) against the salary at the previous year end (e.g. 31 March 2013). For those members who have left during the year, the year end salary will be that at the date of leaving. For those members who have joined during the year, the previous year end salary will be that at the date of joining.

In the event that a strain has occurred, the Fund will recharge the additional liabilities incurred to you in the form of an additional one-off top up contribution. Assessing and managing pay growth strain on an annual basis means that there will be no nasty surprises resulting from pay awards at the 2016 valuation.

It is important to realise that these additional contributions are not an extra cost of participating in the fund. Any salary strain payments have historically been met via higher ongoing pension contributions (due to a higher salary growth assumption being used) or they have emerged at the next valuation resulting in a funding deficit and caused future contributions to rise.

What if salary increases are less than expected?

It is not permissible under the LGPS Regulations to reduce the level of an employer's contributions between actuarial valuations. You will therefore not be permitted a reduction in your certified contributions as a result of pay increases being less than expected. If, however, a pay award gain is calculated in one year, then we would allow this to offset a strain occurring in any future year up to the next formal valuation date. If the overall impact of salary increases between valuations is a gain, then this will be credited to you in your balance sheet position at the next valuation and this will help to reduce your contribution rate going forward (all other things being equal).