

Warwickshire Pension Fund 2019 valuation

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10 December 2019

This presentation has been prepared for discussion at the Warwickshire Pension Fund Academy Meeting on 10 December 2019 only. It should not be used or relied upon for any other purpose.

What are we going to cover?

1. Valuation introduction
2. Valuation assumptions – what's changed?
3. Setting employer rates – what's changed?
4. Results – whole fund
5. Results – employer level
6. Teachers' Pension Scheme – what's going on?
7. Accounting update
8. National hot topics

Please ask questions as we go along

Quiz – It's Christmas!

1. What is the record number of Christmas cards sent by a single person in a year?
 - a) 856
 - b) 5,832
 - c) 62,824
2. How much wrapping paper is sold in the UK every Christmas
 - a) 1,670 acres
 - b) 8,750 acres
 - c) 20,500 acres
3. What speed does Santa travel at to reach every house in the world on Christmas eve?
 - a) 970,000 mph
 - b) 2,340,000 mph
 - c) Speed of light

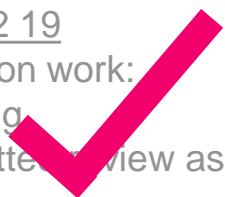
Valuation introduction

2019 valuation timeline

Q4 18 – Q2 19

Pre-valuation work:

- Planning
- Committee review assumptions



July/August 2019

Data cleansed and submitted to actuary
Actuarial calculations processed



September 2019

Committee review whole fund results



November 2019

Finalise employer results
AGM

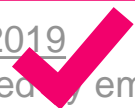


March 2020

Final report signed off by 31 March
Final FSS signed off by Committee

April - June 2019

Data submitted by employers



September 2019

Whole Fund results calculated



October 2019

Initial individual employer results calculated



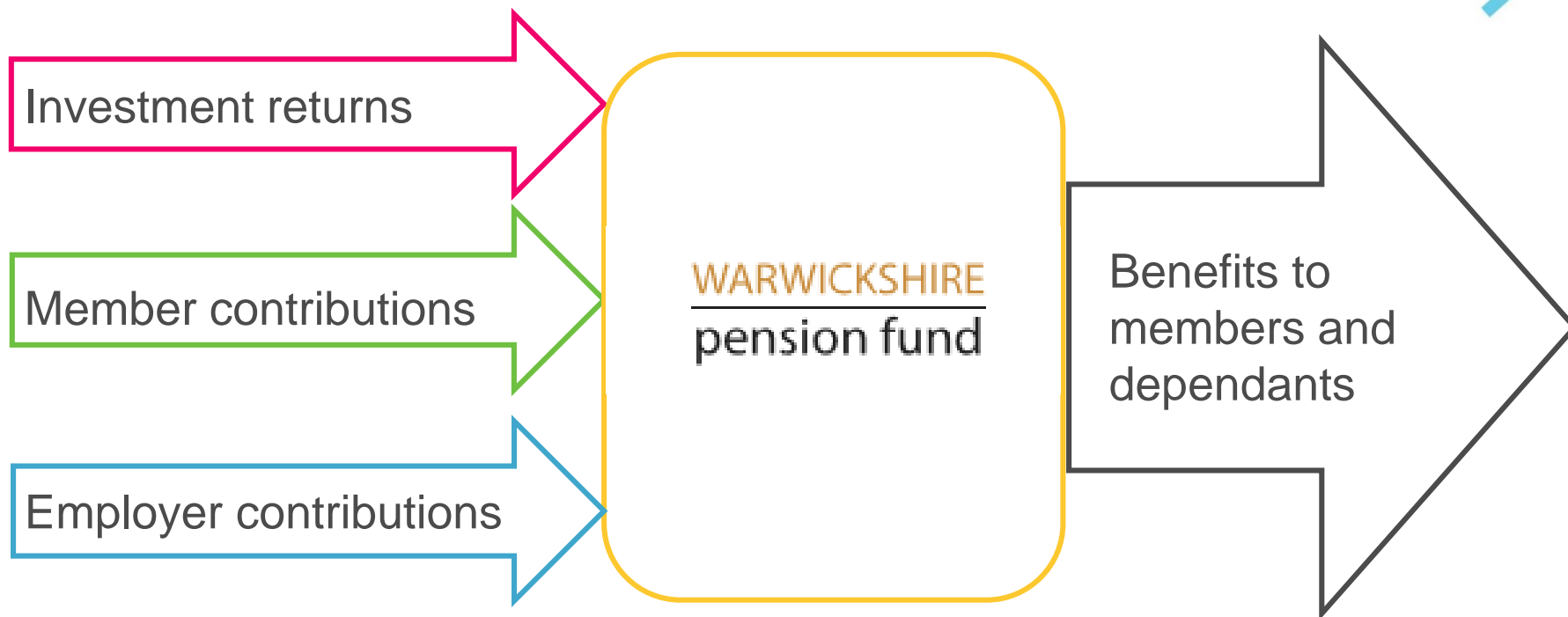
December 2019

Individual employer results issued to employers alongside draft FSS
Pension committee review draft FSS
Academy meeting

1 April 2020

New employer contributions start to be paid

How the Fund works

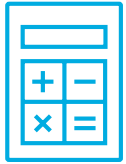


Determined by investment strategy & manager performance

Determined by LGPS Regulations

Must meet balance of cost over longer term

Why we do a valuation



- Calculate employer contribution rates



- Compliance with legislation



- Analyse actual experience vs assumptions



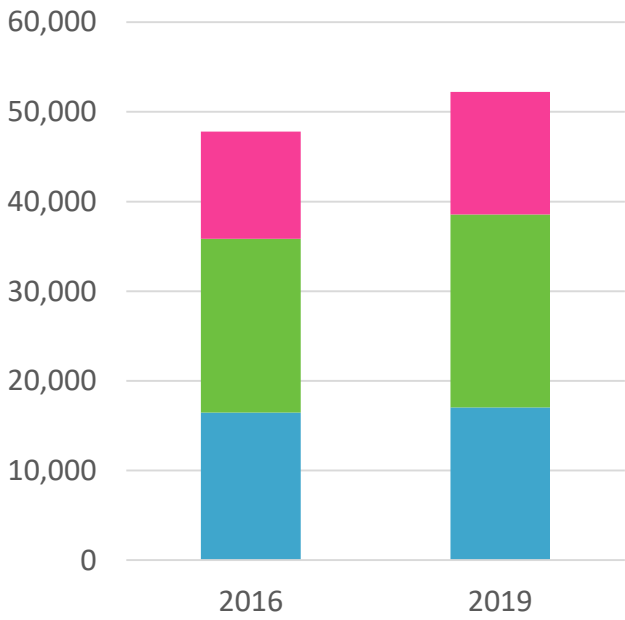
- Review Funding Strategy Statement



- Part of continual 'health check' on fund solvency

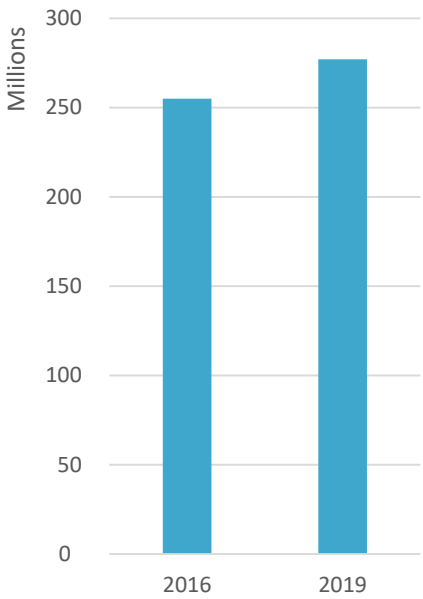
Membership data received and validated

Membership of the Warwickshire Pension Fund



- Pensioners
- Deferred Pensioners
- Actives

Payroll of actives



Pension amounts



- Deferred pensions
- Pensions

The fund has continued to grow in size, increased burden on the admin team

Valuation assumptions – what's changed?

How to fund benefits

Liabilities

Benefits
earned in
future

Benefits
earned to
date

Assets

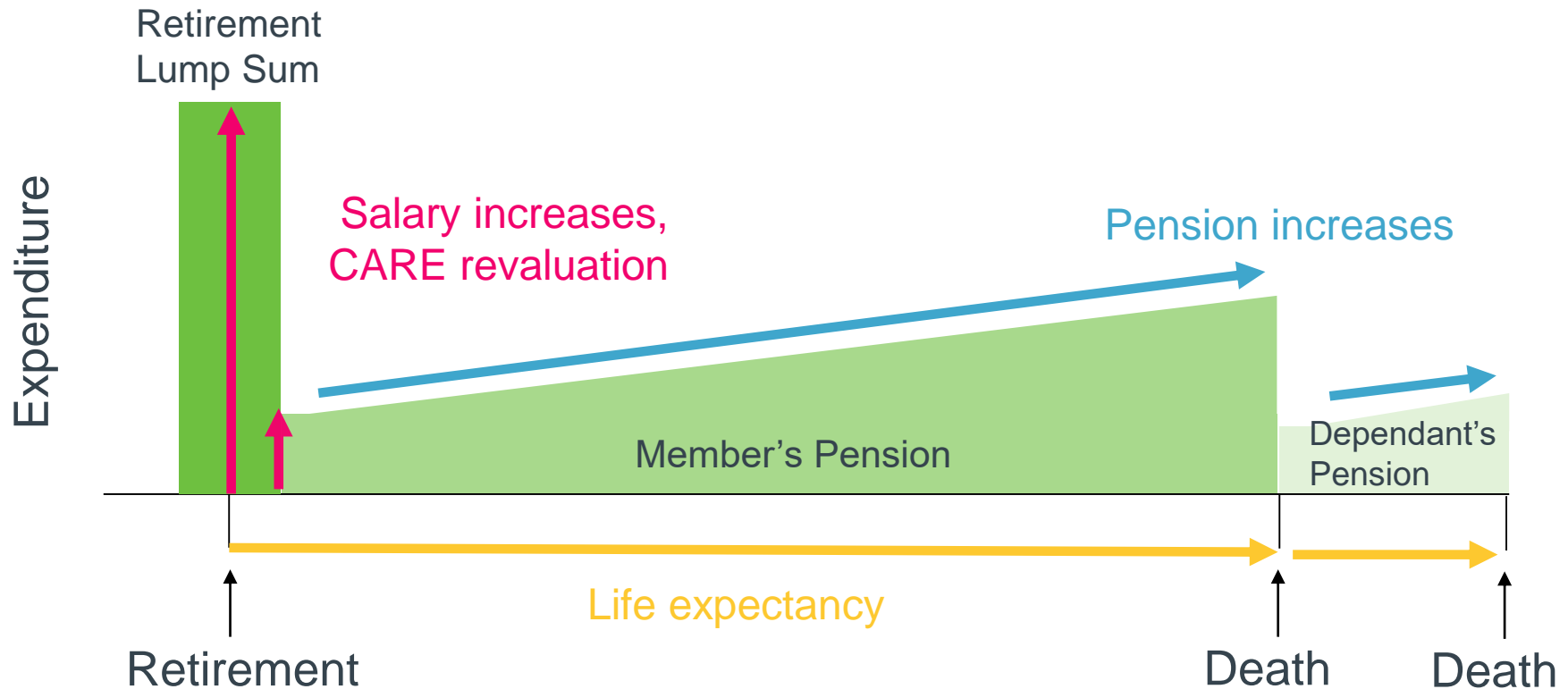
Future
investment
performance

Future
contributions

Assets
today

The purpose of a valuation is to review each of these sections and set a prudent plan to pay each member's benefits

Why do we need assumptions?



Recap: 2016 funding plan

2016

Benefits
earned in
future

Liabilities
(Benefits
earned to
date)

Future
investment
performance

Future
contributions

Assets today

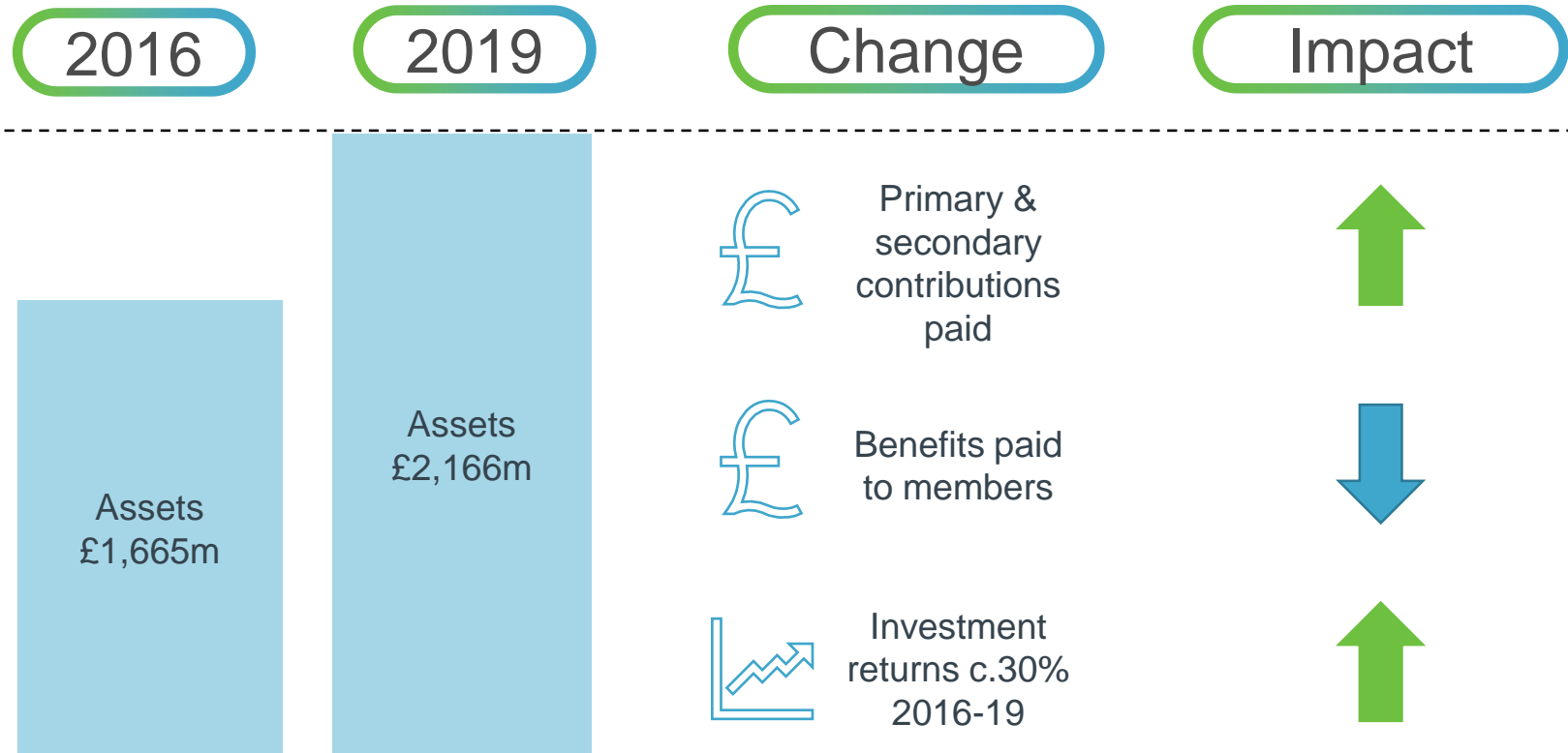
3.8% p.a.

Primary: 20.0% of pay
Secondary: £8,440,000

Funding level 82%

The key valuation decision is the balance of contributions and investment performance

What has happened to the Fund's assets between 2016-2019?



What is the outlook for the return on the assets the Fund holds?

2016

2019

Change

Impact

3.8% p.a.

3.7% p.a.

Assets have increased in price

Price increases mean assets now cost more

When assets cost more, outlook for returns is lower

What has happened to the benefits you need to fund?

2019

Change

Impact

Benefits earned in future

Liabilities (Benefits earned to date)



Future pay increases



Life expectancy



GMP indexation



McCloud judgement





Future pay increases

Then

BBC Sign in News Sport Weather iPlayer Sounds

NEWS

Home UK World Business Politics Tech Science Health Family & Education

Business Your Money Market Data Companies Economy

Budget 2013: Public sector pay rise cap extended

© 20 March 2013

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A 1% pay rise cap for public sector workers will be extended for an extra year to 2015-16, Chancellor George Osborne has announced.

The move comes as some civil servants stage a one-day strike over pay and pensions.

Mr Osborne said that public sector pay would be limited to an average of 1% including in 2015-16.



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Public sector workers 'to get above-inflation pay rise'

© 19 July 2019

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Hundreds of thousands of public sector workers are reportedly in line to get a pay rise.

Long-term pay increase assumption up from 0.6% to 0.8% above CPI inflation



Falling life expectancy makes headlines

The Actuary

The magazine of the Institute & Faculty of Actuaries

Falling life expectancy to slash pension scheme liabilities

sky news

A lot of people in the City are getting very excited about death

“...£2bn windfall to the life sector.”

MailOnline

British life expectancy falls by SIX MONTHS for men and women with experts blaming NHS cuts and a rise in dementia, diabetes and obesity

“...pension firms have already began to cash in on falling life expectancies.”

THE WALL STREET JOURNAL.

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MARKETS | HEARD ON THE STREET

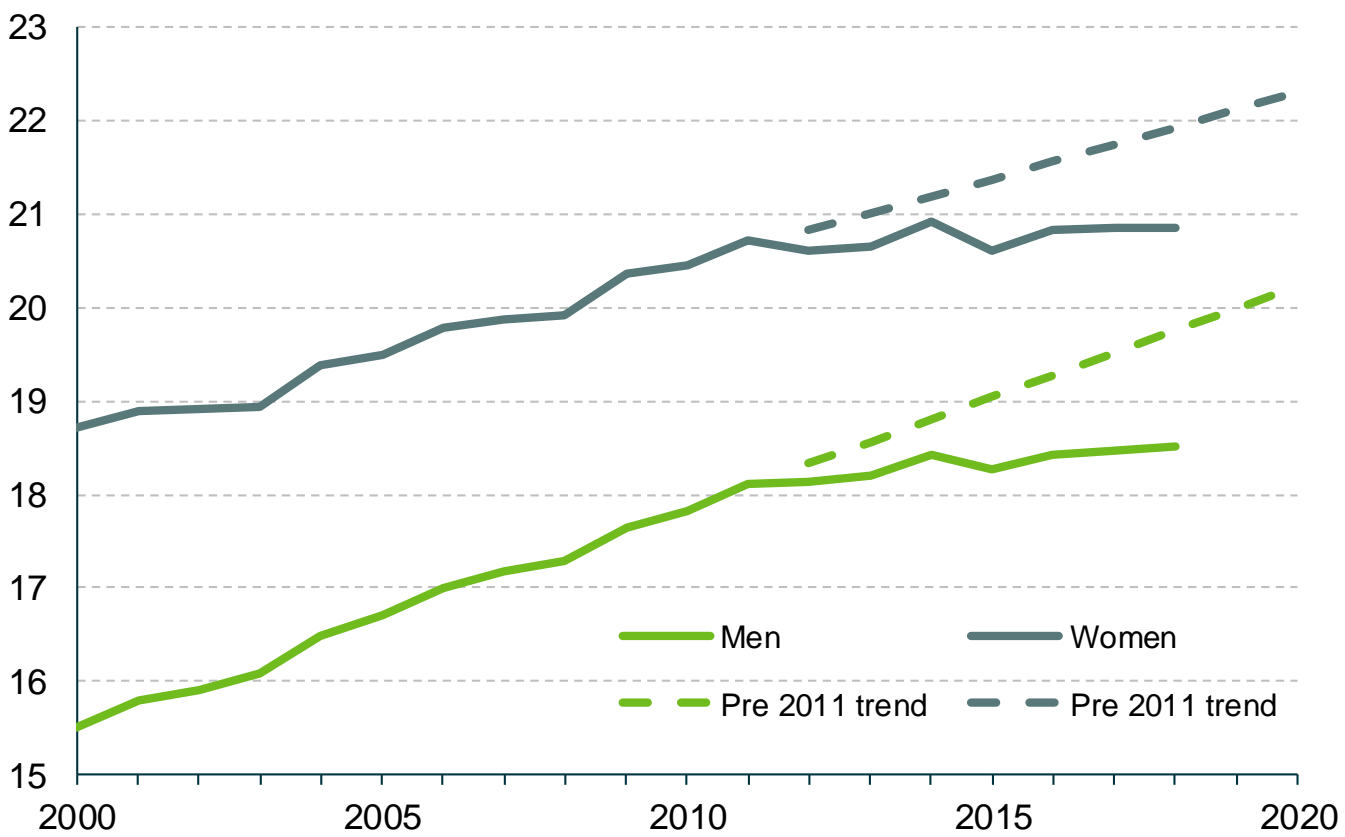
Life Was Short for Longevity Gains

Life expectancy at 65 is falling and that means cash windfalls for insurers



Is it fake news?

Period life expectancy from age 65



True for the general population...



Not the same for everyone



Group	Annualised mortality improvement (age-standardised)		
	2001-2006	2006-2011	2011-2016
General Population	3.0% (±0.1%)	2.6% (±0.1%)	0.9% (±0.1%)
Comfortable	2.0% (±0.6%)	2.6% (±0.4%)	1.5% (±0.4%)
Making-Do	2.9% (±0.4%)	2.9% (±0.3%)	1.1% (±0.3%)
Hard-Pressed	2.6% (±0.4%)	3.1% (±0.3%)	0.7% (±0.3%)

Still improving

Slowing down

Typical LGPS Fund Profile

Lives - male



10-15% of members...

Liabilities - male



...50% of liabilities

- Hard Pressed
- Making Do
- Comfortable
- Unknown

Less impact than the headlines suggest



GMP: Generating More Problems



State pension age before 2016

Baseline GMP funded by LGPS employers

Annual increases funded by combination of LGPS employers and central government

Overall GMP + state pension equal between men and women

State pension age after 2016

Baseline GMP funded by LGPS employers

Annual increases **entirely** funded by LGPS employers

Overall GMP + state pension equal between men and women

Potential increase to liabilities depending on your membership

Many employers will see no impact at all

McClouds on the horizon

Apr
2014/5

Reforms to public service pensions following Hutton review – benefits generally made less generous but older members are spared

➔ Members launch legal challenge claiming age discrimination

Jan
2017

➔ Government loses and appeals to Court of Appeal

Dec
2018

Court of Appeal rules against the Government

➔ Government appeals to Supreme Court

June
2019

Supreme Court declines to hear the Government's appeal

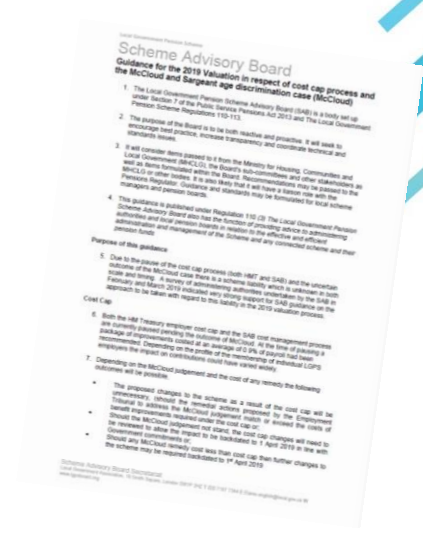
???

Significant uncertainty over public sector pension benefits (and costs)



Impact on 2019 valuation

- What benefit structure to value?
 - Actuaries should value the current benefits*
- How will the fund manage the risk over benefit structure uncertainty?
 - Increase prudence when setting rates via higher likelihood of meeting the funding target
- Can funds revisit rates after the valuation once the case is resolved?
 - Yes
- What about employers leaving the fund?
 - If you leave the fund before the case is resolved, you may be asked to pay more to cover the potential cost of improved benefits



2019 funding plan

2019

Benefits
earned in
future

Liabilities
(Benefits
earned to
date)

Future
investment
performance

Future
contributions

Assets today

3.7% p.a.

Broadly similar to current levels

Funding level 92%

No significant change to assumptions since the last valuation


“No news is good news!”

Setting employer rates – what's changed?

Recap: how we calculate contributions

2013 and before


What is the funding target? 


How long do we want to give the employer to get to the target? 

What single set of assumptions are we going to use?

2016 onwards

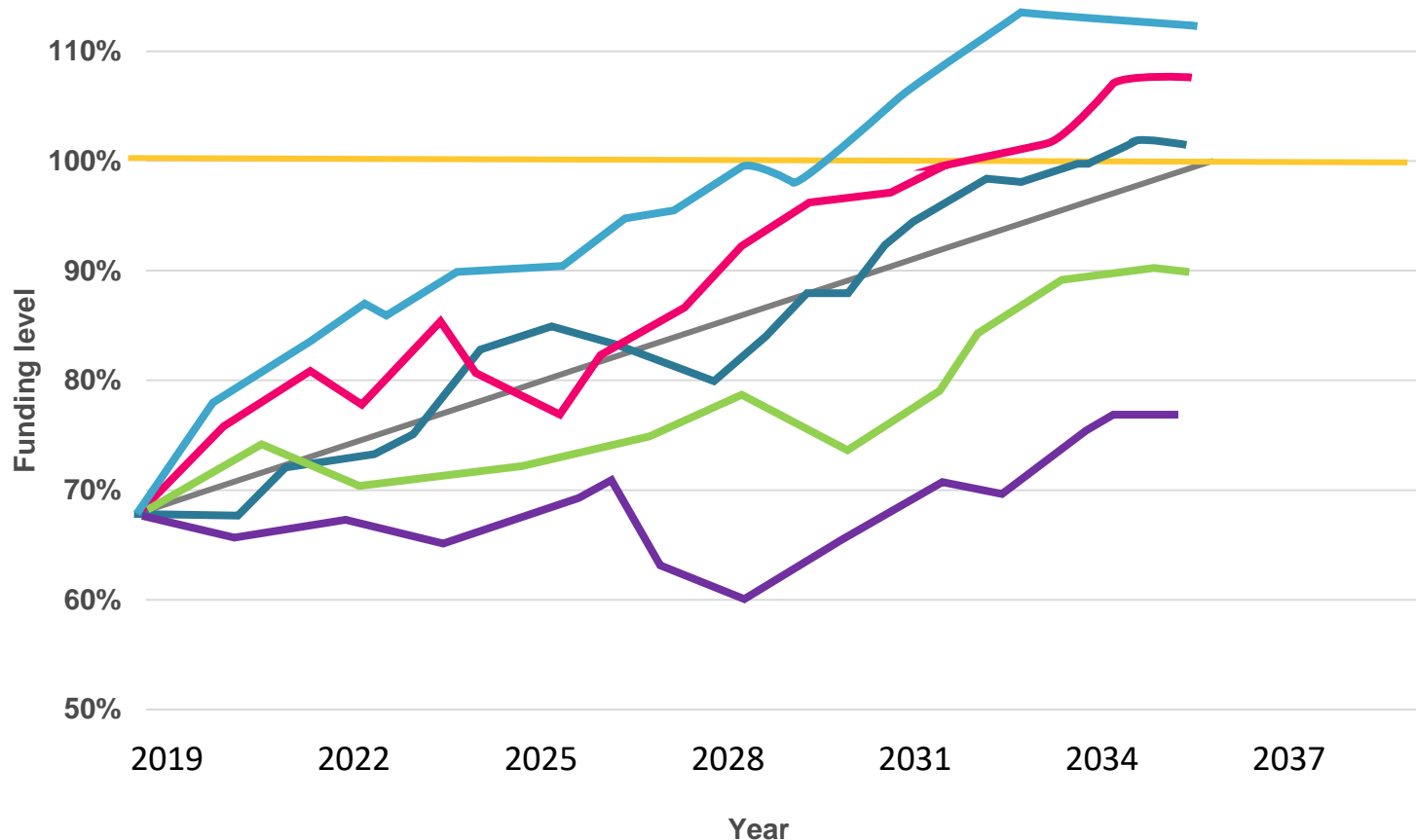
What is the funding target? 

How long do we want to give the employer to get to the target? 

How sure do we want to be that the employer hits the target? 

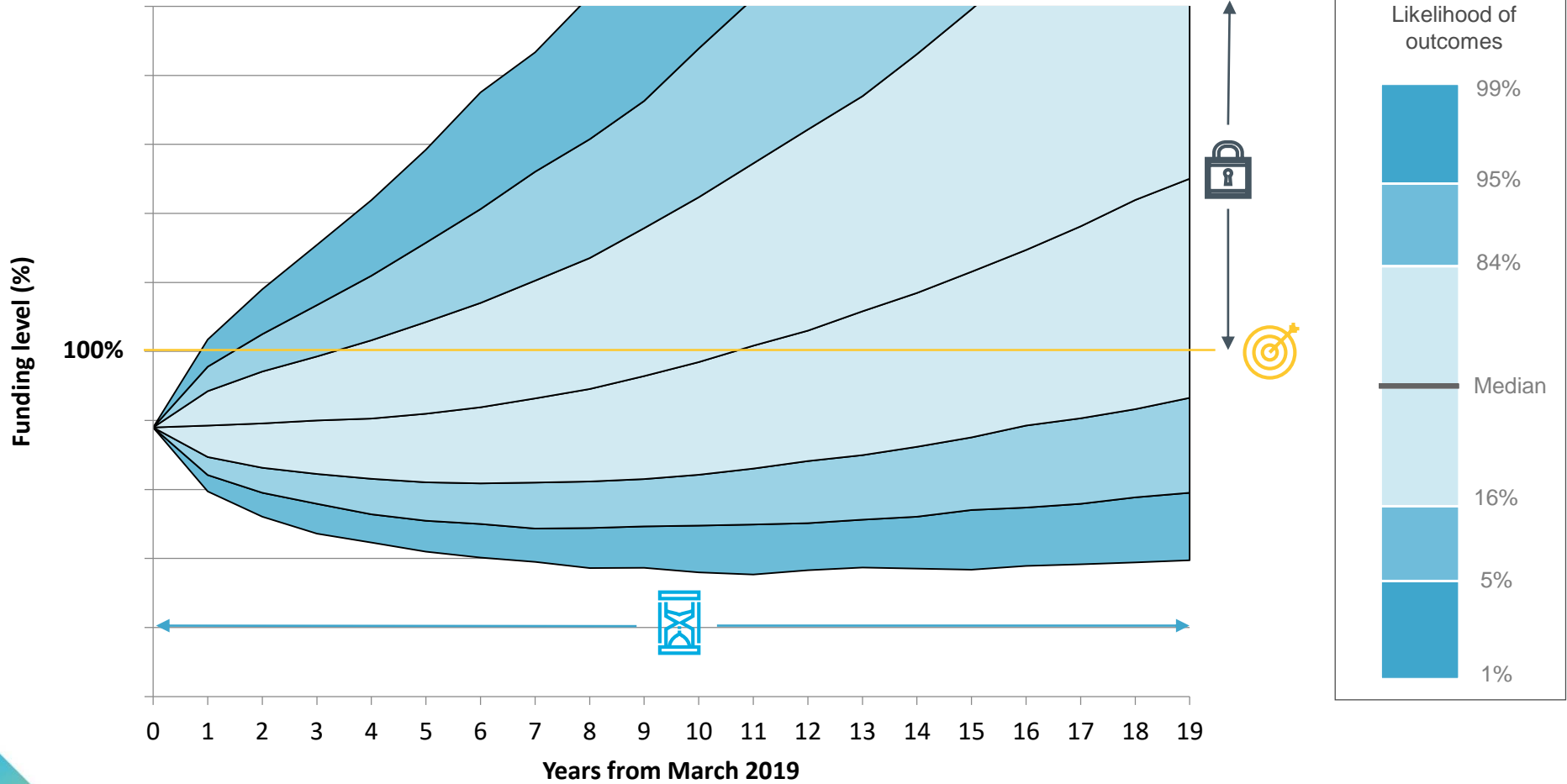
The method for setting contribution rates allows for future uncertainty and helps all stakeholders understand the risk inherent in funding plans

Test contributions under thousands of economic scenarios



Each scenario has different inflation, investment returns, interest rates etc

Combining it all together



Set a contribution rate so that enough outcomes are 'successful'

2016 valuation: funding strategy



Employer type	Ultimate Funding target	Time horizon	Likelihood of success	Stabilised contributions
Councils and Police	Ongoing	Long – 19 years	66%	Yes
Academies	Ongoing	Long – 19 years	66%	No
Colleges	Ongoing	Long – 19 years	75%	No
Transferee Admission Bodies	Ongoing	Short – contract length	66%	No
Community Admission Bodies	Cessation	Medium/Short	75%	No

Ensuring funding strategy is appropriate for each employer group

2019 valuation: funding strategy



Employer type	Ultimate Funding target	Time horizon	Likelihood of success	Stabilised contributions
Councils and Police	Ongoing	Long – 19 years	70%	Yes
Academies	Ongoing	Long – 19 years	70%	No
Colleges	Ongoing	Long – 19 years	80%	No
Transferee Admission Bodies	Ongoing	Short – contract length	70%	No
Community Admission Bodies	Cessation	Medium/Short	80%	No

Not much change
Higher likelihoods applied to cover emerging risks
at this valuation

Focus on academy funding strategy

How are contribution rates are expressed?

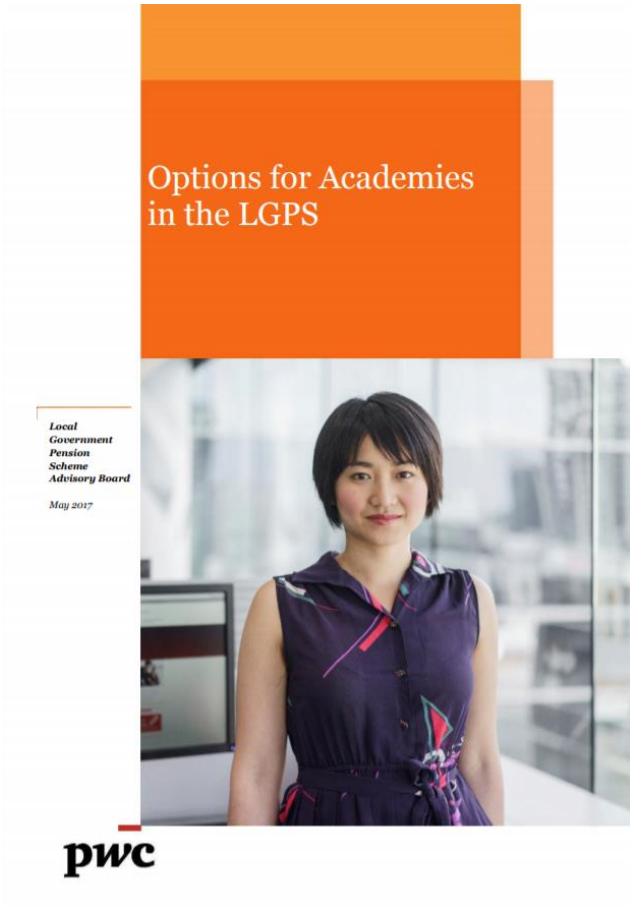
- 2016 valuation
 - Primary rate expressed as a percentage of pay
 - Secondary rate expressed as an annual monetary amount
- 2019 valuation
 - Total rate expressed as a percentage of pay

What contribution rate is paid by academies in a MAT?

- Same contribution rate paid by all academies in a MAT
- Individual academy funding positions are tracked

Aim of making administration as simple
as possible for Fund and Academies

SAB review of academies



- Published May 2017
- Review of issues faced by academies in the LGPS
- Three emerging key themes
 1. Policy & governance
 2. Administration
 3. Contributions and finance
- Next steps focussing on administration
- No impact on contributions

Where to find further information



Funding Strategy Statement details the Fund's approach to funding benefits for all employers and managing risks

Results— whole fund

Whole Fund funding position - change

	2016 valuation (£m)	2019 valuation (£m)
Active liabilities	736	809
Deferred pensioner liabilities	409	503
Pensioner liabilities	878	1,033
Total liabilities	2,023	2,346
Assets	1,665	2,166
Surplus/(Deficit)	(358)	(180)
Funding level	82%	92%

Funding level shows a snapshot on one particular day,
but funding pension benefits is a long term game

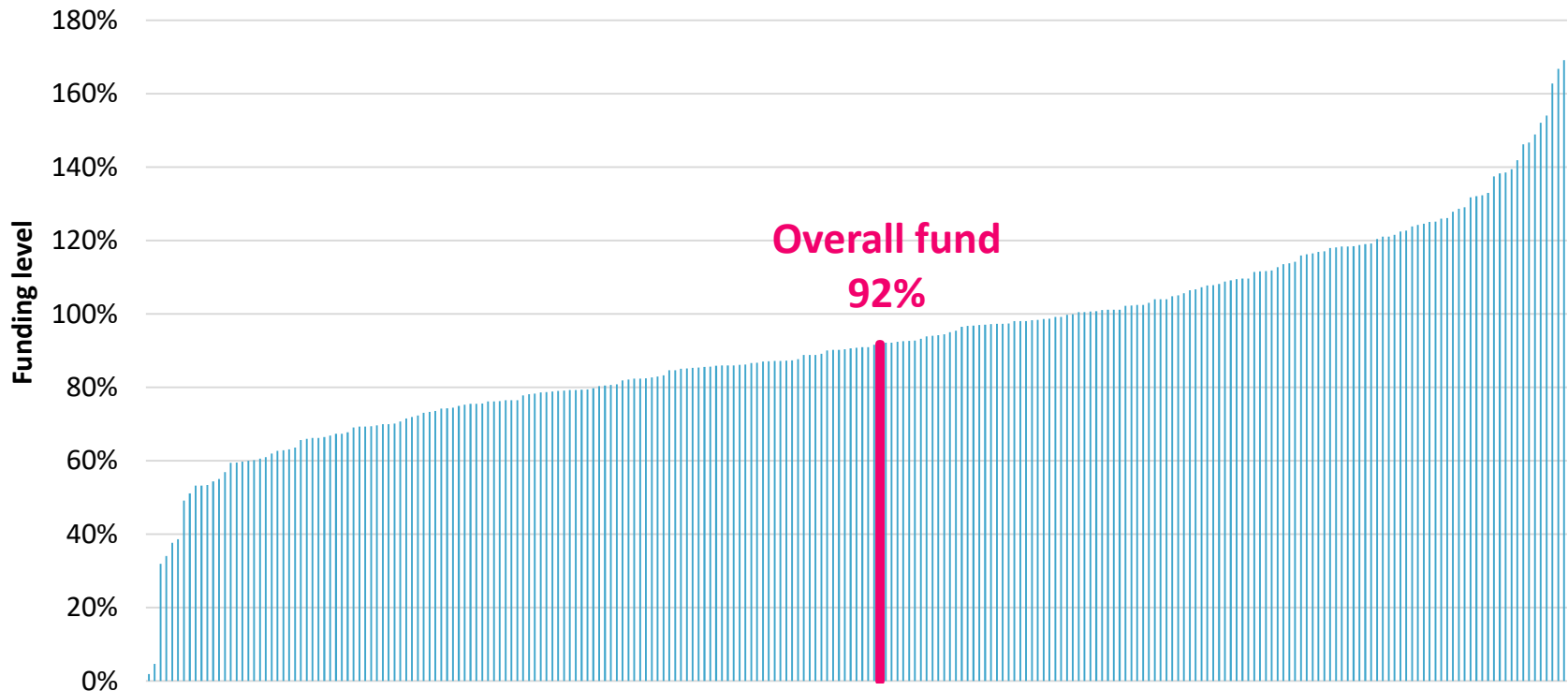
What's changed since 2016?

Change in value (£m)	Assets	Liabilities	Surplus / (Deficit)
Last valuation – 31 March 2016	1,665	2,023	(358)
Cashflows			
Employer contributions paid in	167		167
Employee contributions paid in	51		52
Benefits paid out	(223)	(223)	0
Net transfers into / out of the Fund	7		7
Other cashflows (e.g. expenses)	(6)		(6)
Expected changes in membership			
Interest on benefits already accrued		242	(242)
Accrual of new benefits		251	(251)
Membership experience vs expectations			
Salary increases less than expected		(1)	(1)
Benefit increases less than expected		(0)	0
Early retirement strain & contributions	0	17	(17)
Ill health retirement strain		(9)	9
Early leavers less than expected		(2)	2
Pensions ceasing greater than expected		4	(4)
Commutation less than expected		0	(0)
Impact of GMP equalisation		3	(3)
Other membership experience		(8)	8
Change in market conditions			
Investment returns on the Fund's assets	505		505
Changes in future inflation expectations		67	(67)
Changes in actuarial assumptions			
Change in demographic assumptions		(5)	5
Change in longevity assumptions		(67)	67
Change in salary increase assumption		7	(7)
Change in discount rate		47	(47)
This valuation – 31 March 2019	2,166	2,346	(180)

Results— employer level

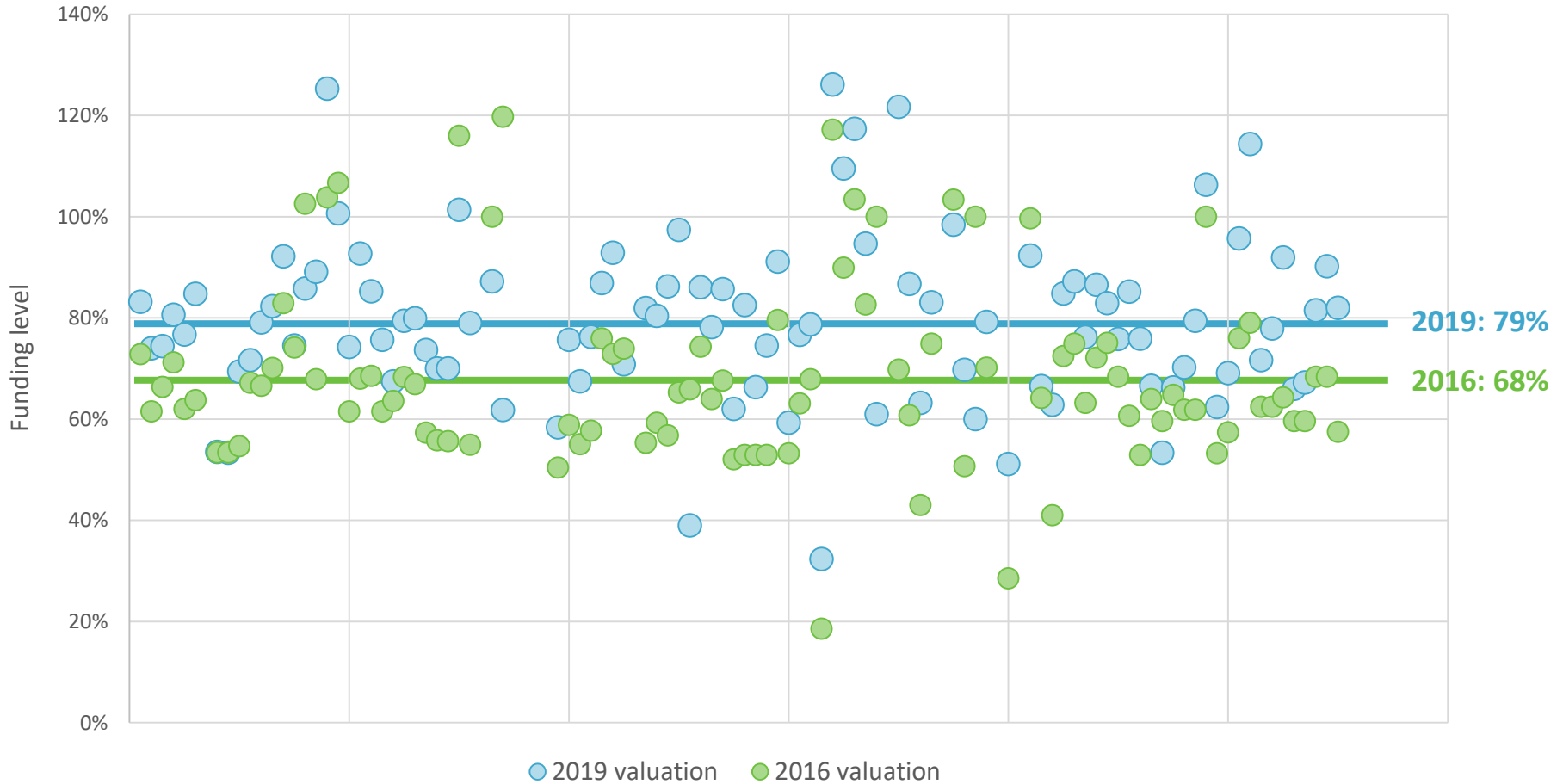
Range of employer funding levels

2019 valuation - distribution of employer funding levels



Most employers will see an improved funding level versus 2016, but there is a wide range

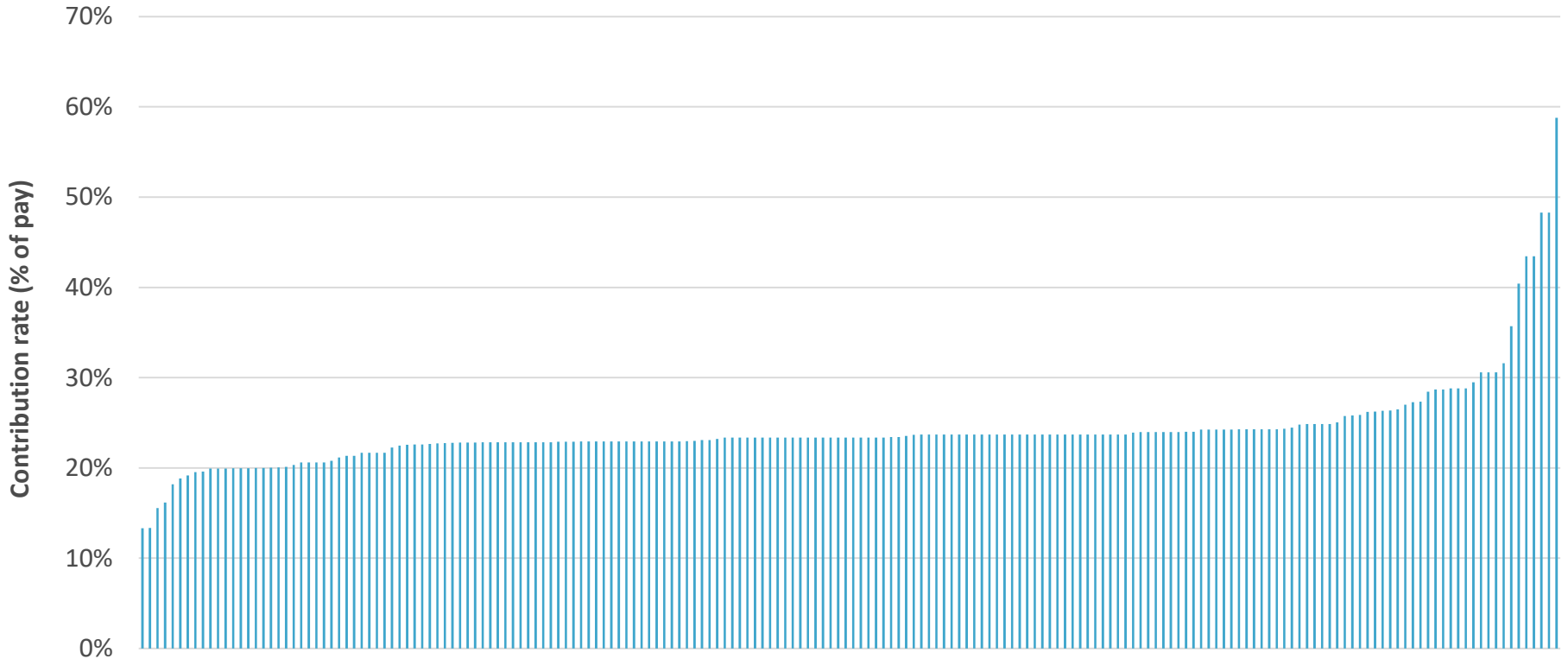
Academies: change in funding level



General improvement in funding position

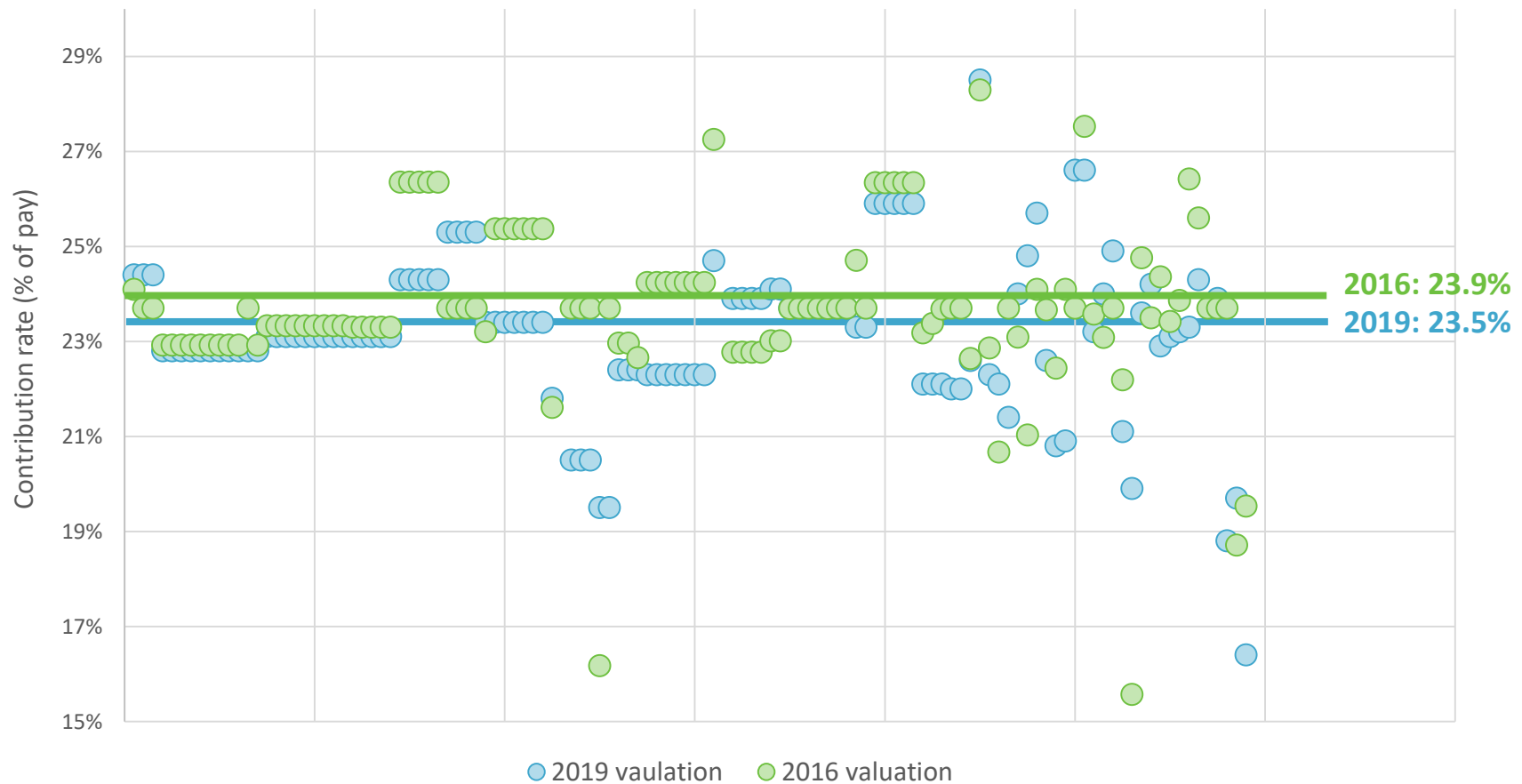
Range of employer contribution rates

Distribution of employer contribution rates



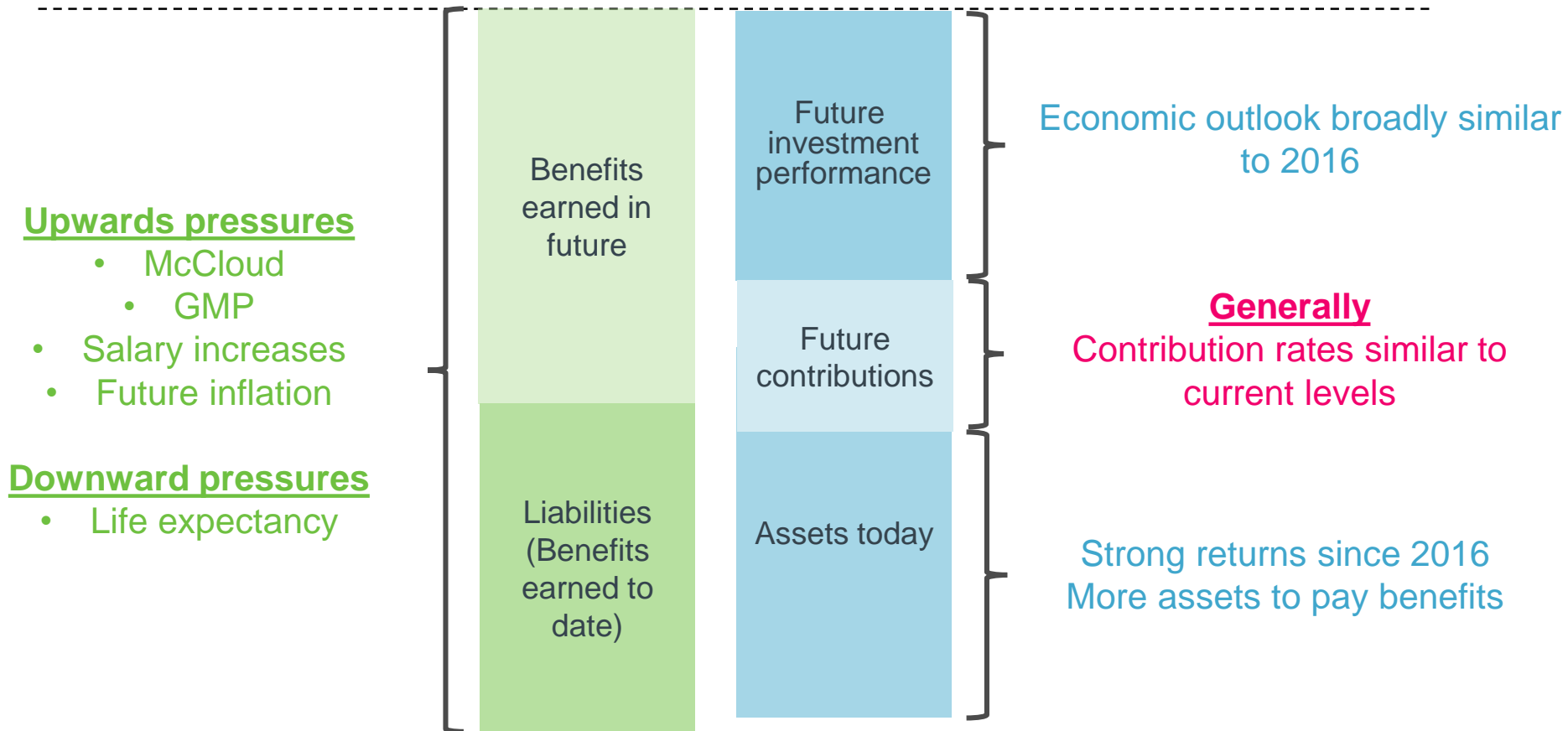
Overall, not much change is expected but will vary between employers

Academies: change in contribution rate



Generally stable contribution rates

Summary



Funding balance sheets generally improved from 2016

Contribution rates generally around the same level

Teachers' Pension Scheme - what's going on?

Current state of play in TPS

Employer contribution rates have risen from 16.5% to 23.7% of pay

Potential increases to member benefits from 1 April 2019

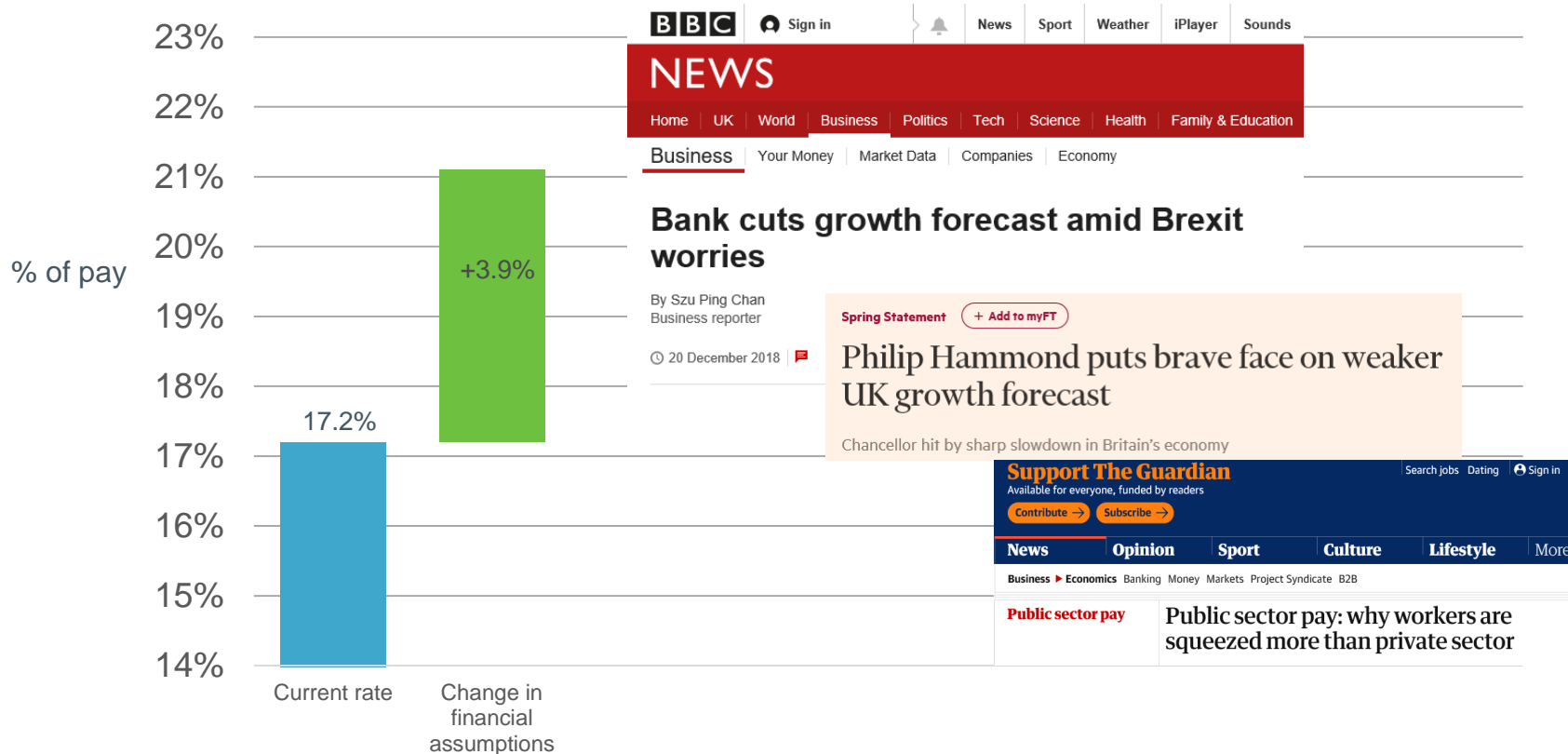
Why are benefit improvements being considered whilst rates are rising?

How has the cost changed?



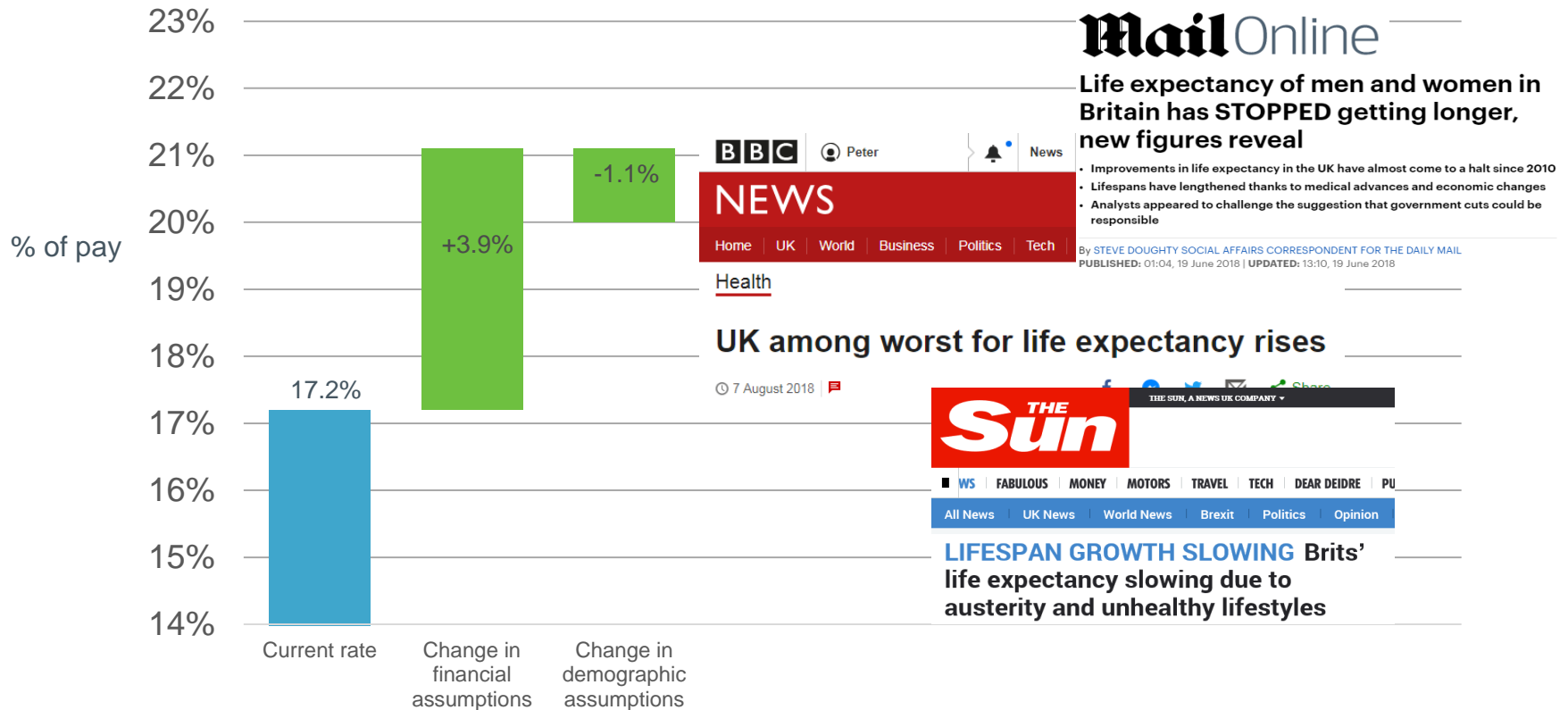
Example: Scottish Teachers Pension Scheme

How has the cost changed?



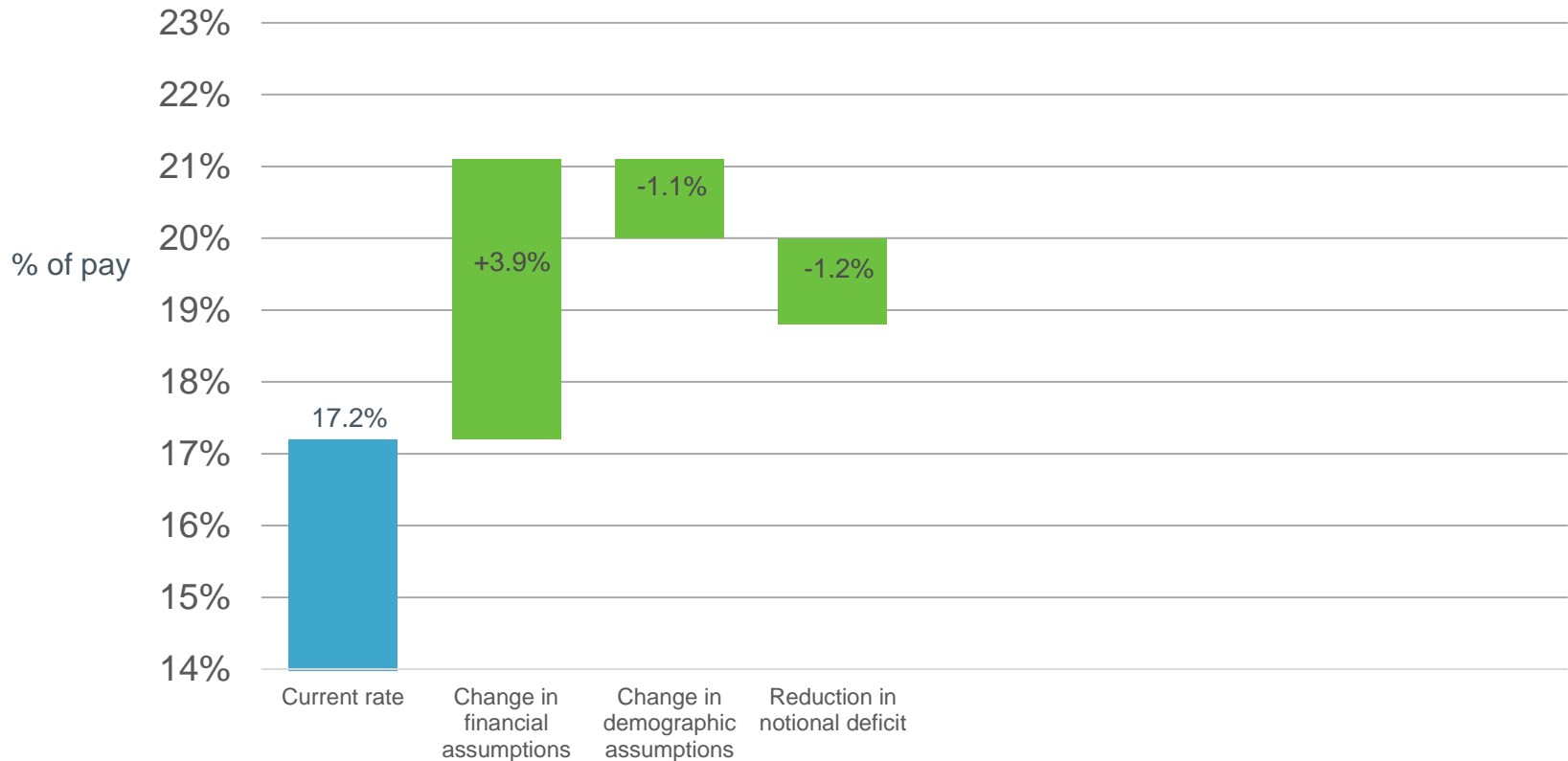
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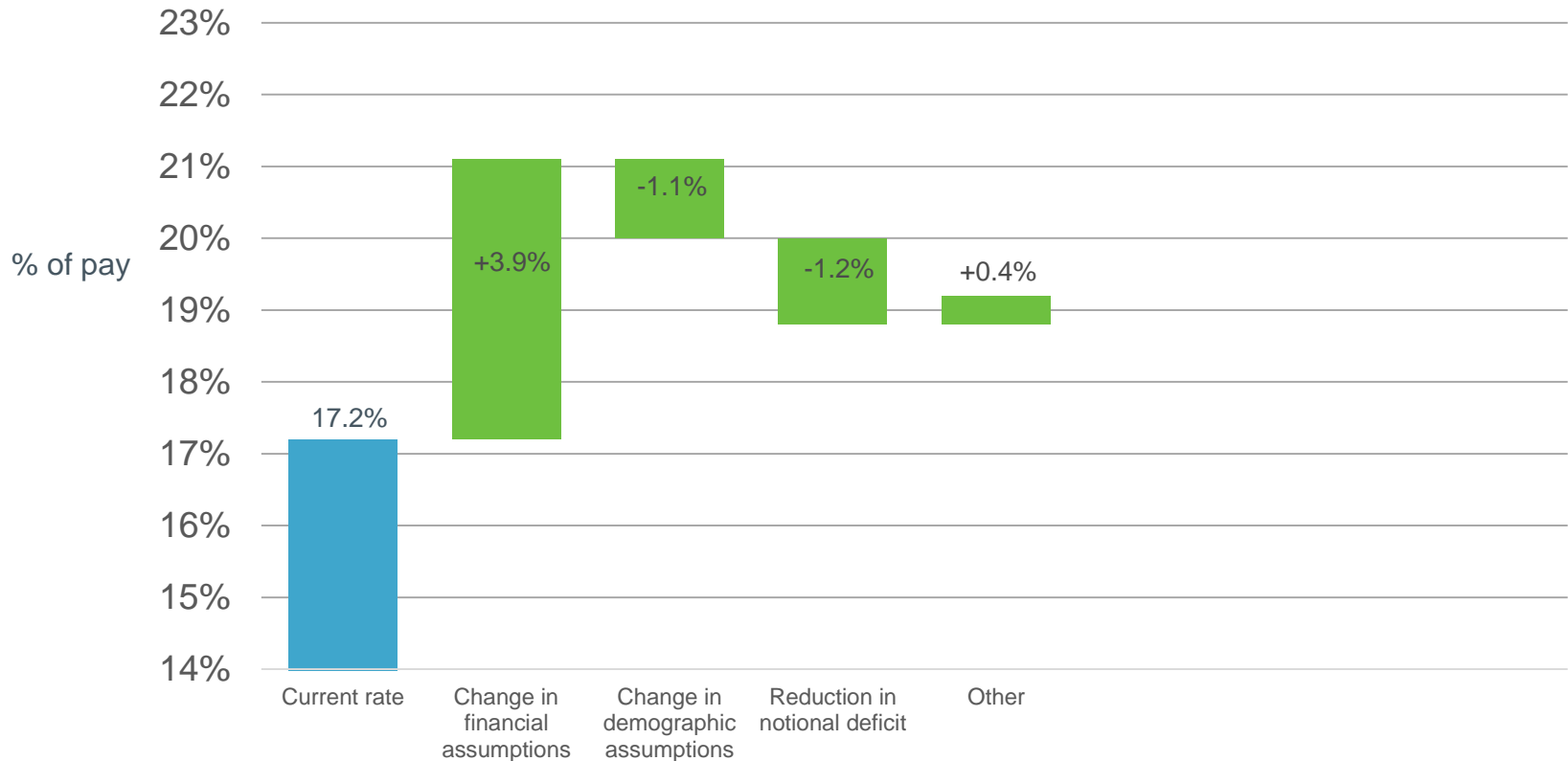
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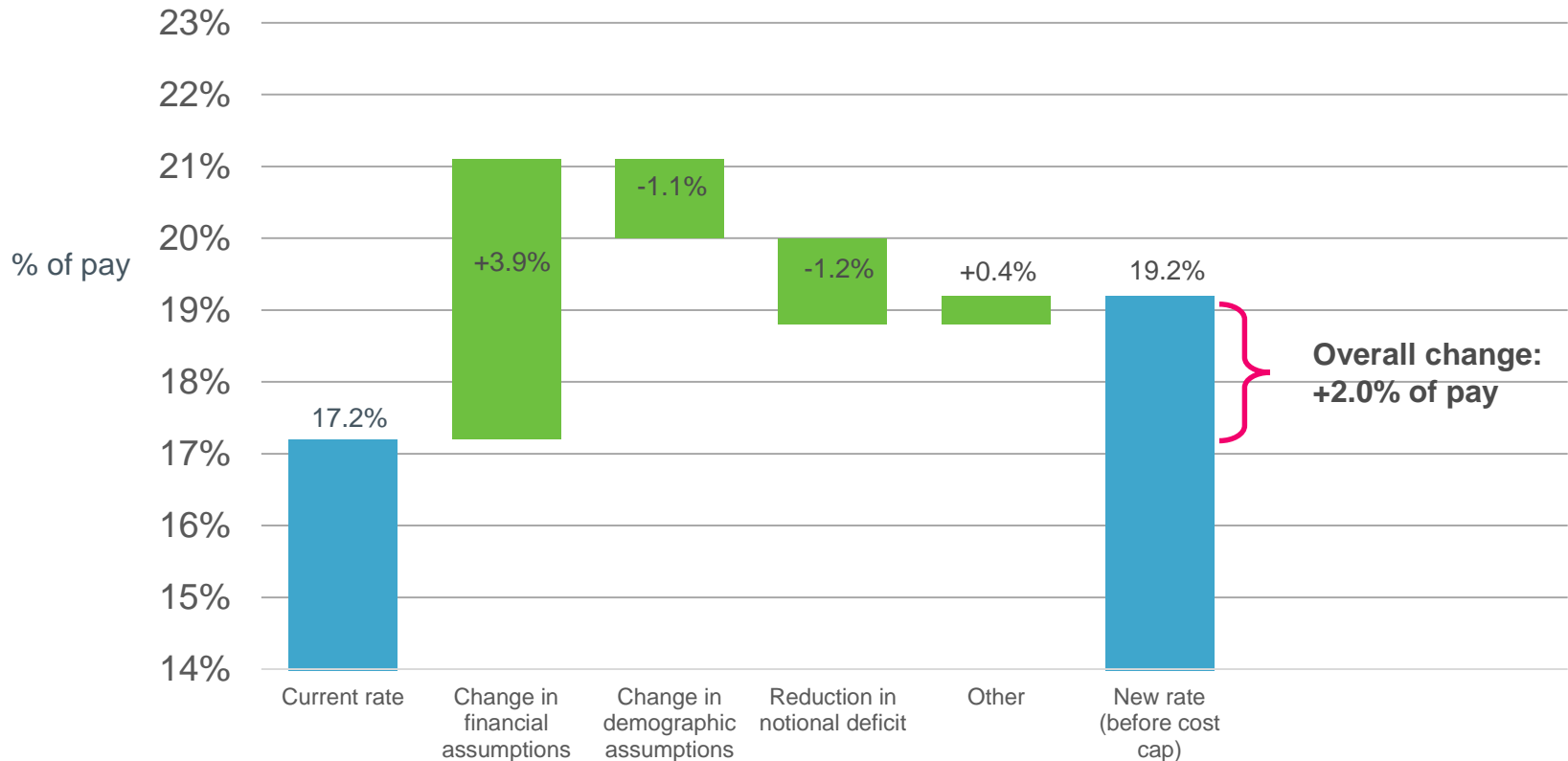
Example: Scottish Teachers Pension Scheme

How has the cost changed?



Example: Scottish Teachers Pension Scheme

How has the cost changed?



Example: Scottish Teachers Pension Scheme

Cost cap: new kid on the block



Independent Public Service
Pensions Commission:
Final Report

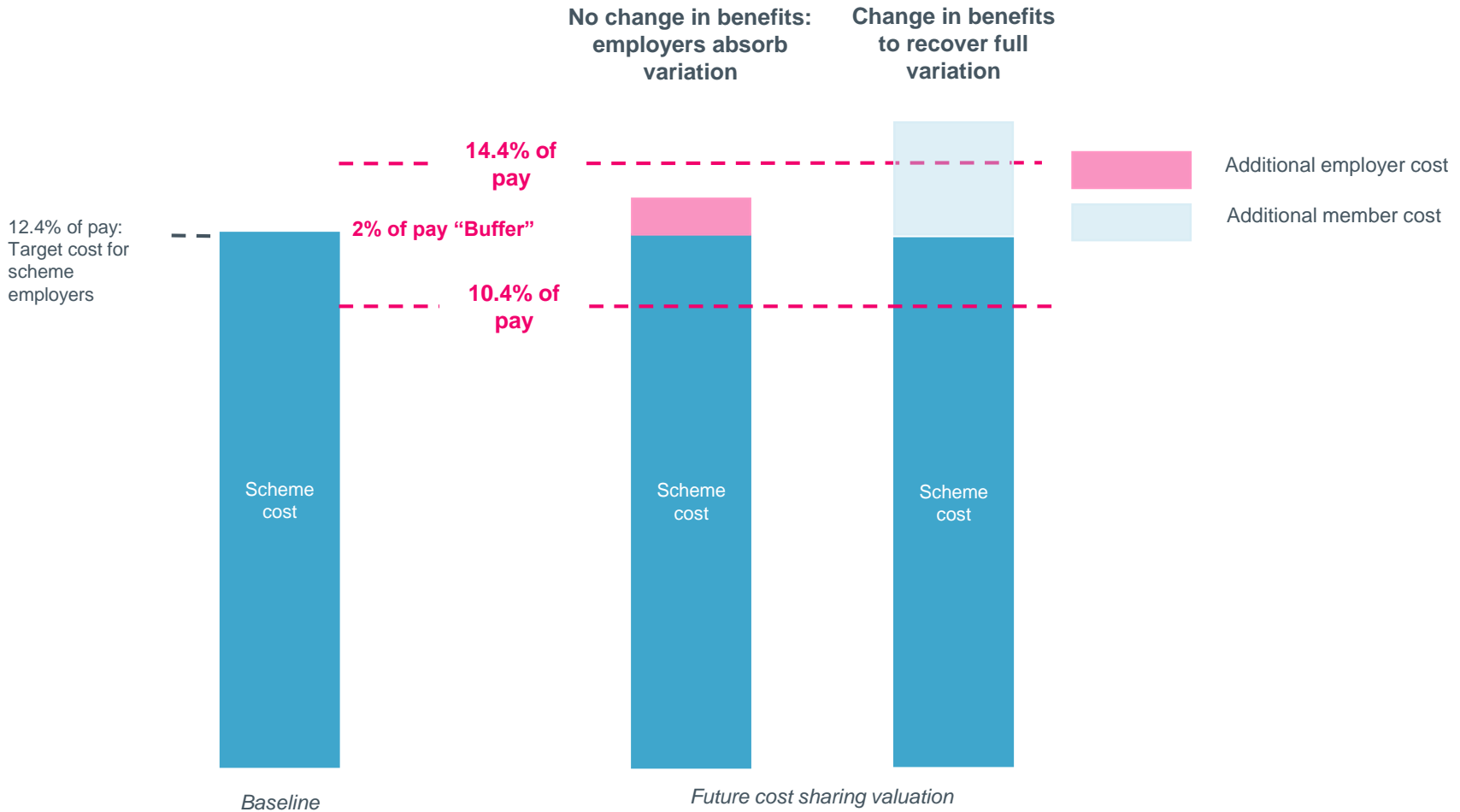
10 March 2011



Recommendation 12: The Government, on behalf of the taxpayer, should set out a **fixed cost ceiling**: the proportion of pensionable pay that they will contribute, on average, to employees' pensions over the long term. If this is exceeded then there should be a consultation process to bring costs back within the ceiling, with an **automatic default** change if agreement cannot be reached.

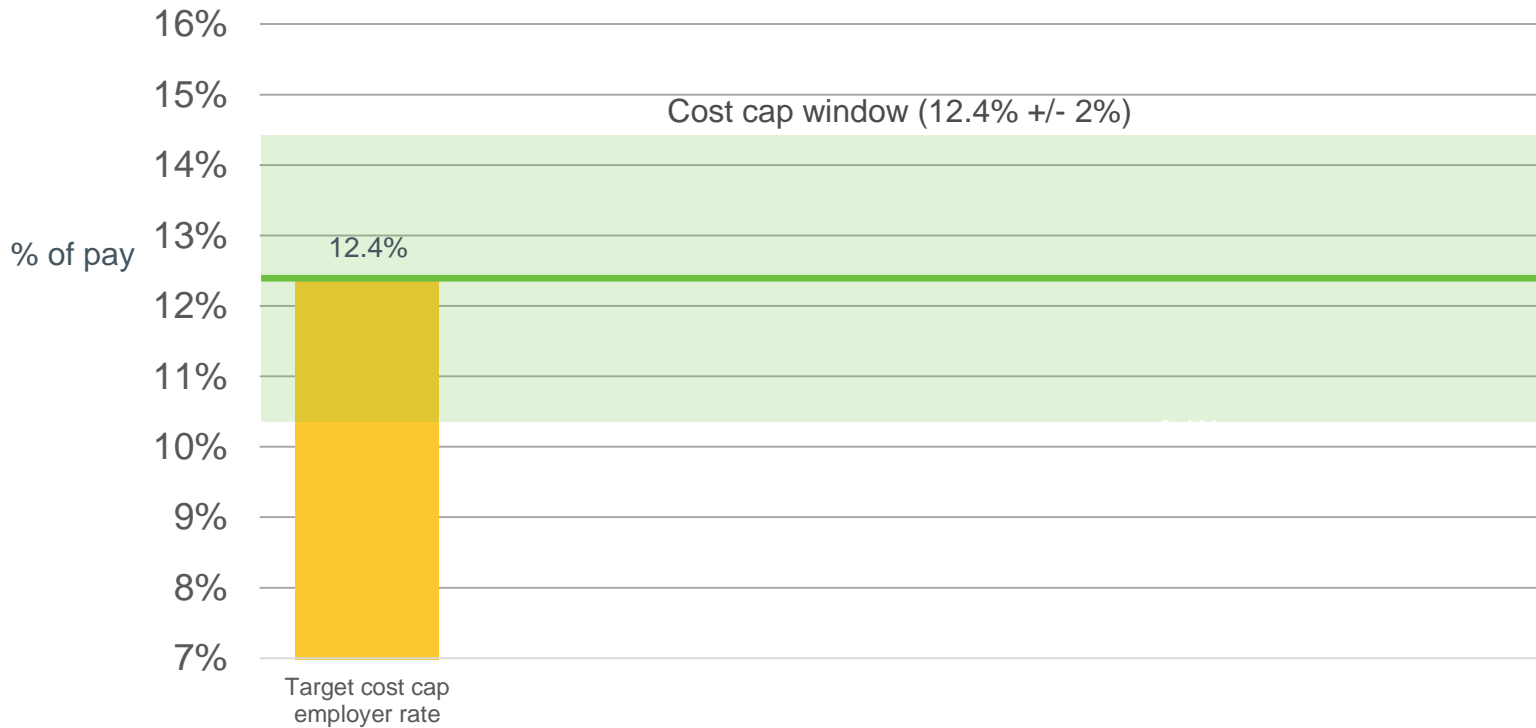
A 'cost cap' mechanism to avoid
unchecked increases in pension costs

How the “Cost Cap” works

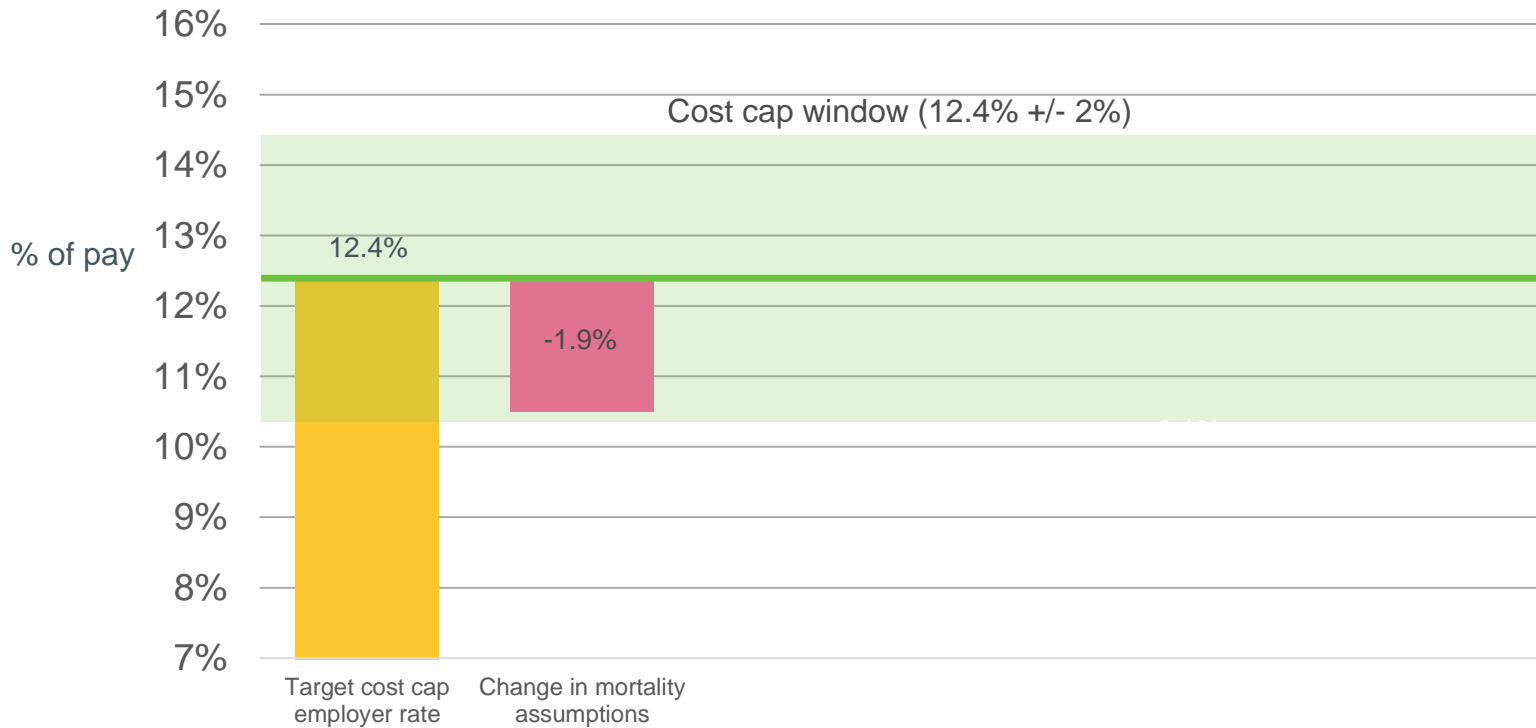


During implementation of reforms, the cost cap became cost sharing

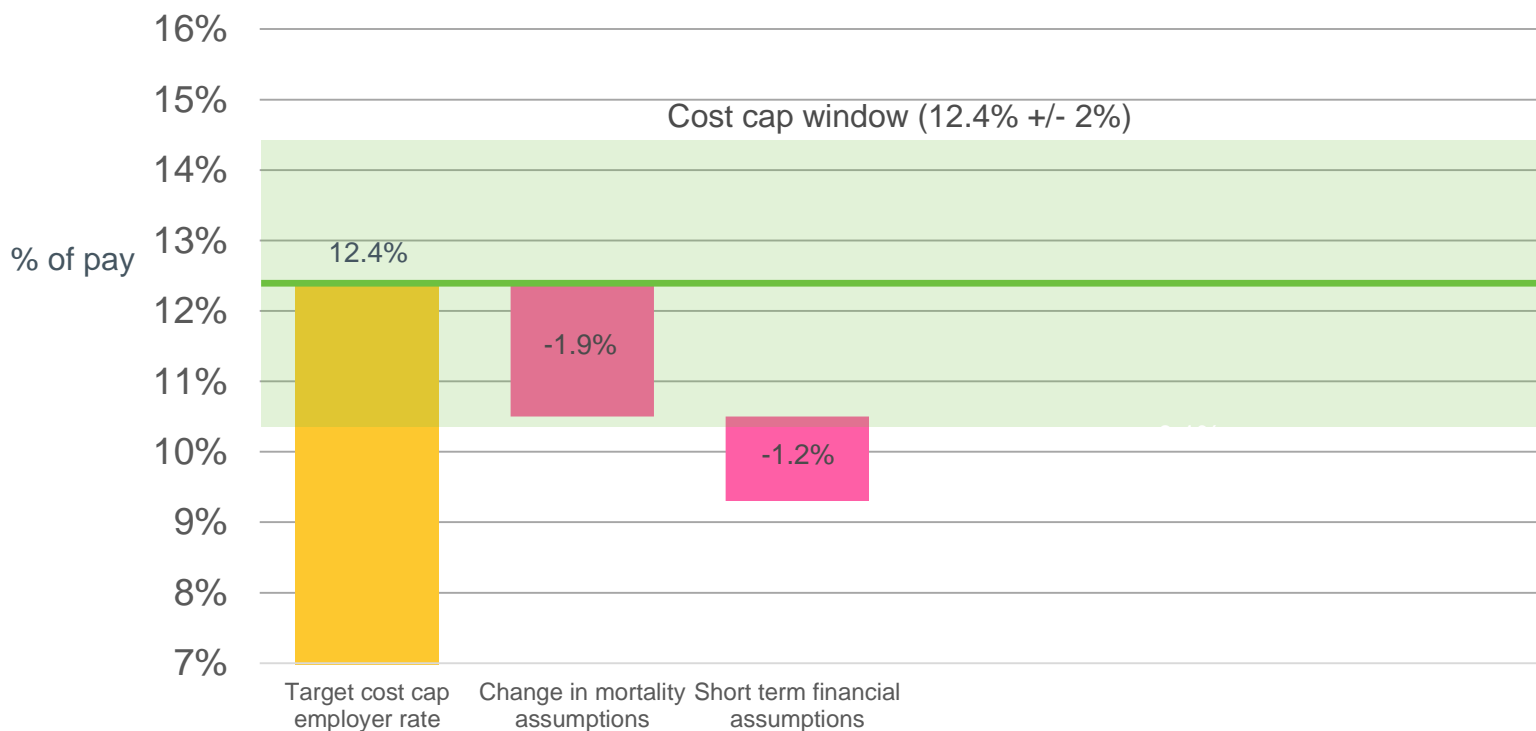
Why are benefits increasing?



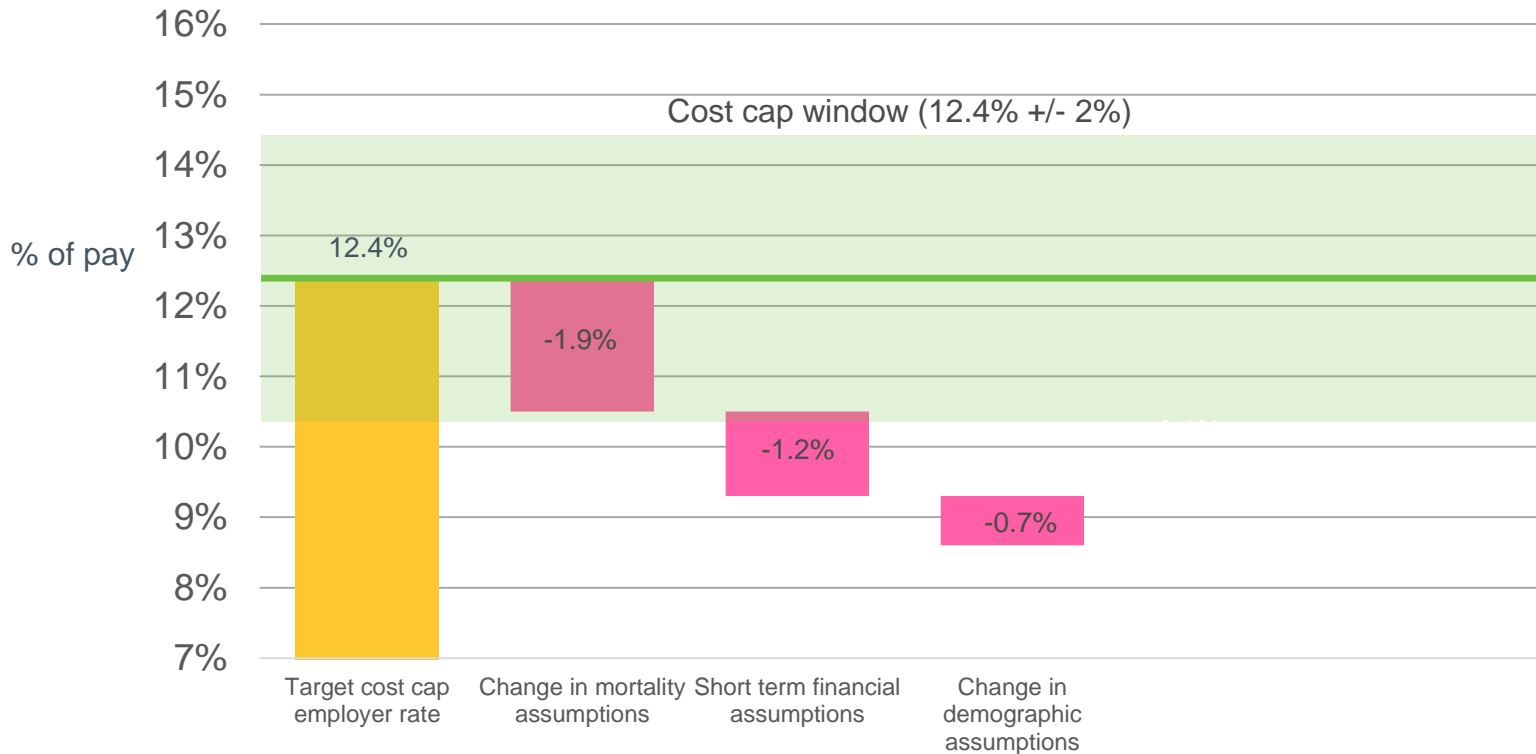
Why are benefits increasing?



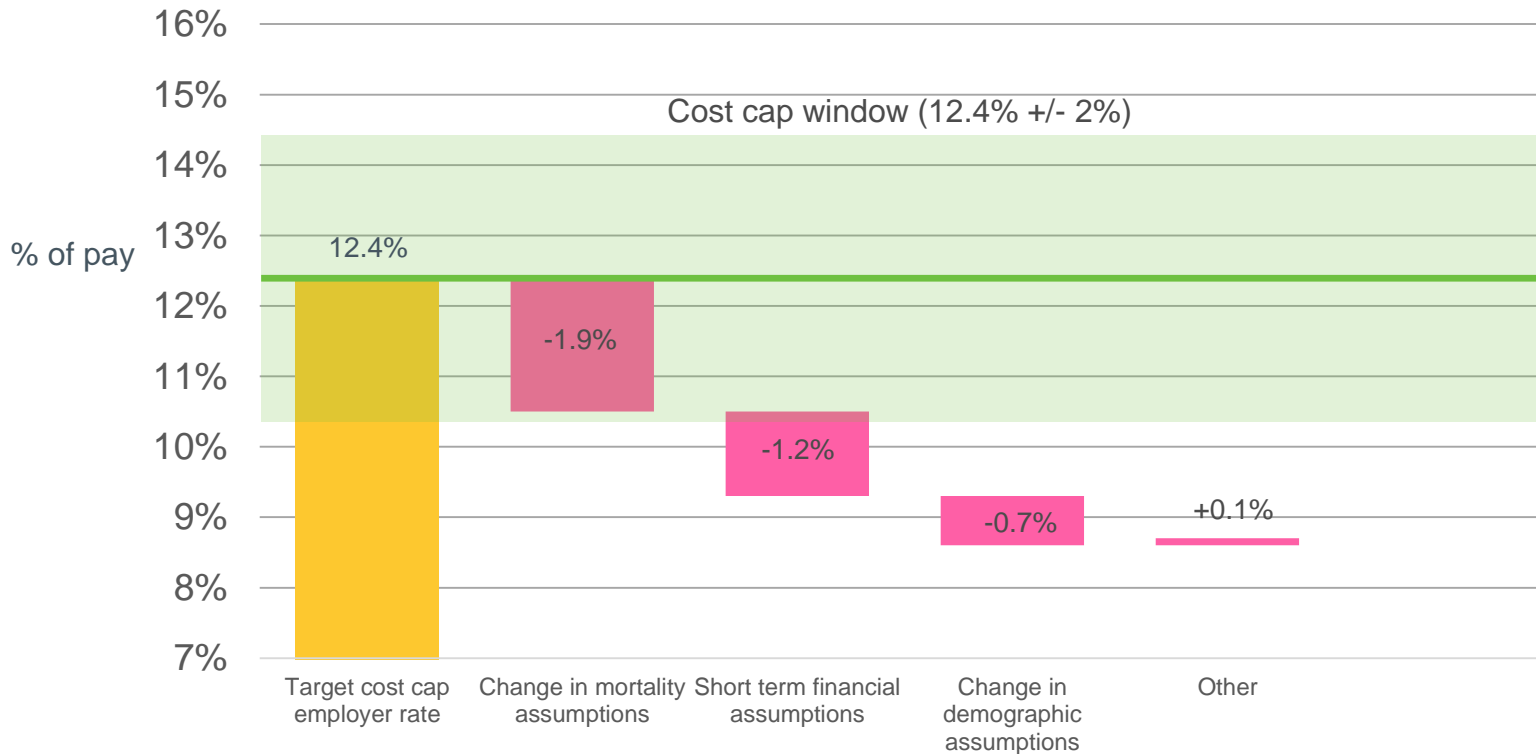
Why are benefits increasing?



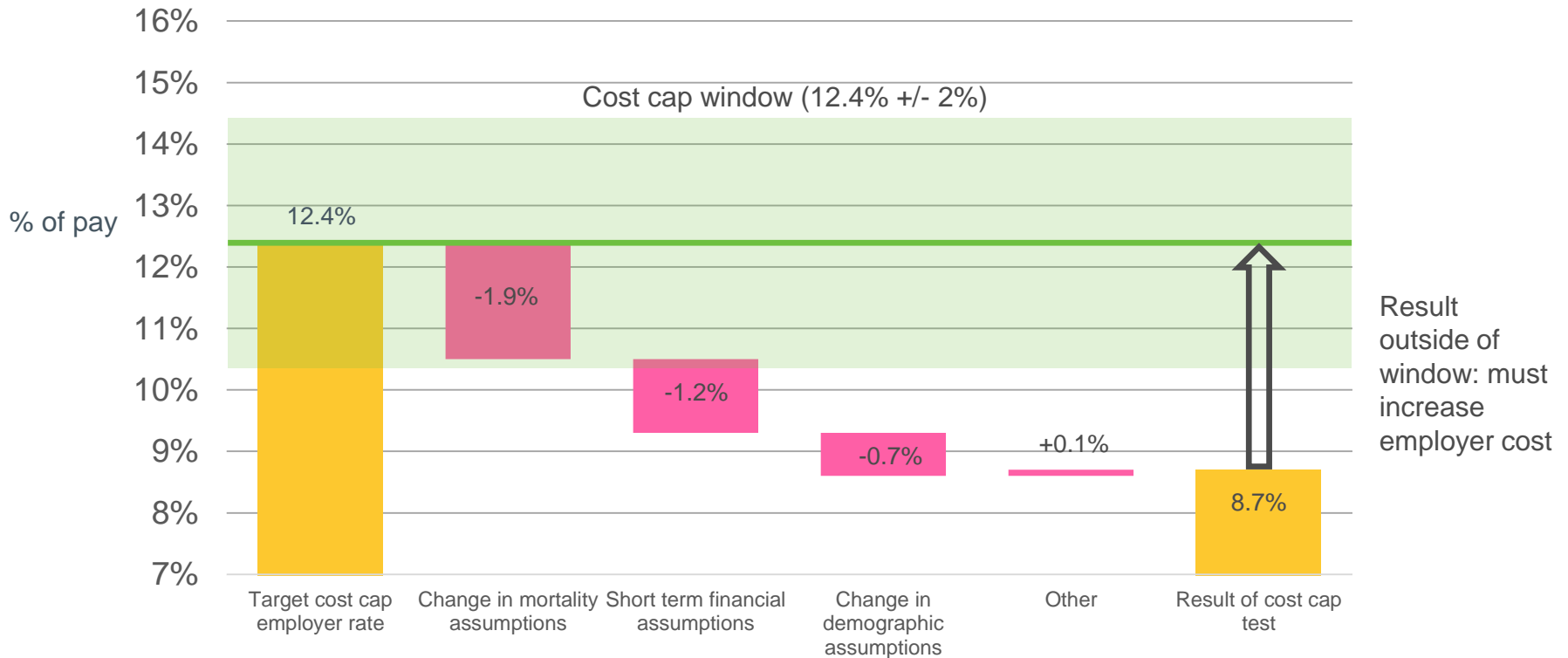
Why are benefits increasing?



Why are benefits increasing?

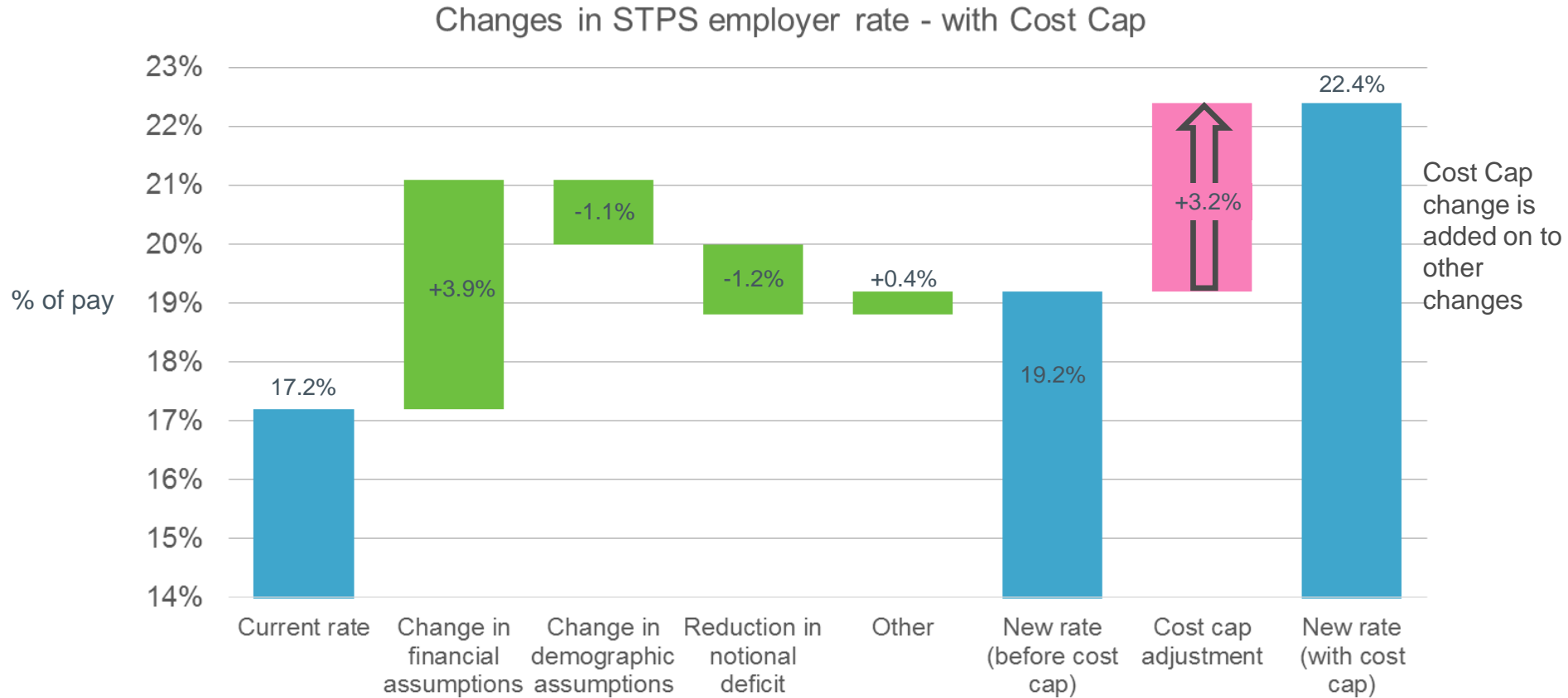


Why are benefits increasing?



Cost cap valuation result requires scheme changes equal to 3.7% of pay

Putting it all together



The Cost Cap offsets all the positive experience

Accounting update

Current accounting themes

Rising balance sheet deficits and P&L items

- Result of reduction in discount rate
- FRS102 specifies how discount rate is set – yield on high quality corporate debt

Allowing for McCloud

- Format of final solution unknown
- Only able to make an educated estimate

Allowing for GMP indexation

- Very small impact – try to avoid spurious accuracy

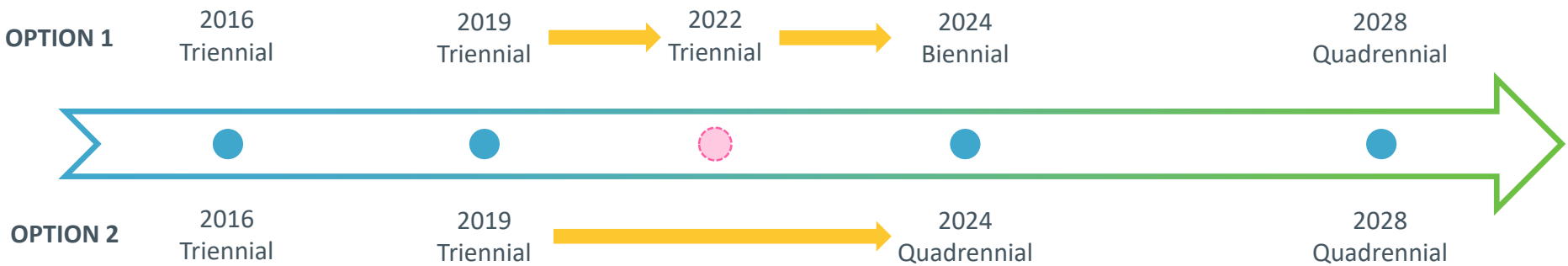
Looking ahead to 2020

- August 2020 reports will be first based on 2019 valuation
- Expect experience items on both assets and liabilities

Refer to supporting documents or ask the Fund

National hot topics

Valuation cycle and management of employer risk

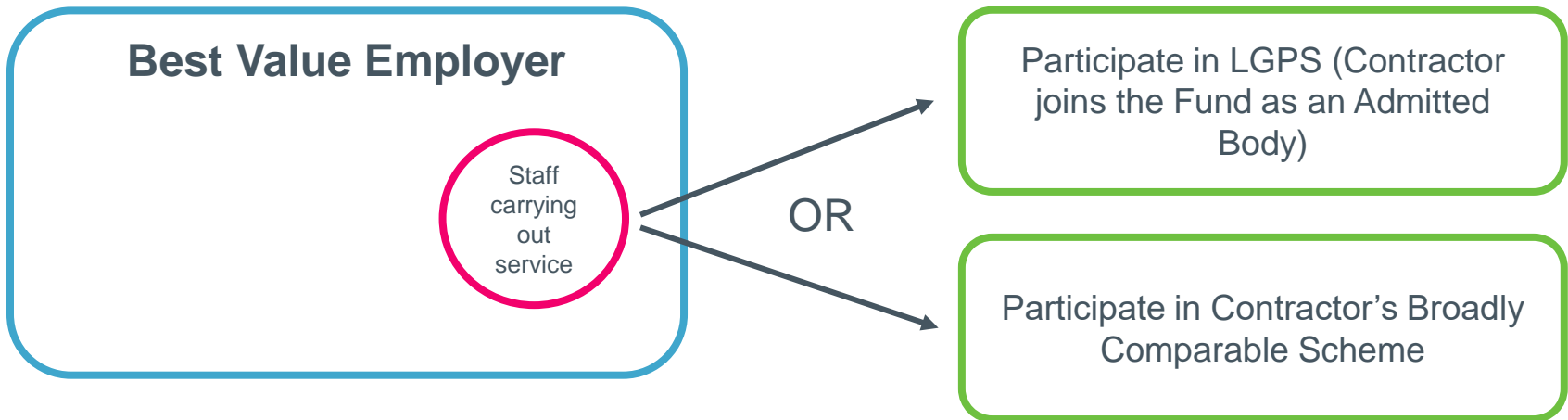


1. MHCLG proposal of flexibility on exit payments
2. Exit credits: consideration of the employer's exposure to risk for exit credits
3. Further Education Bodies: access to the LGPS limited for new employees?

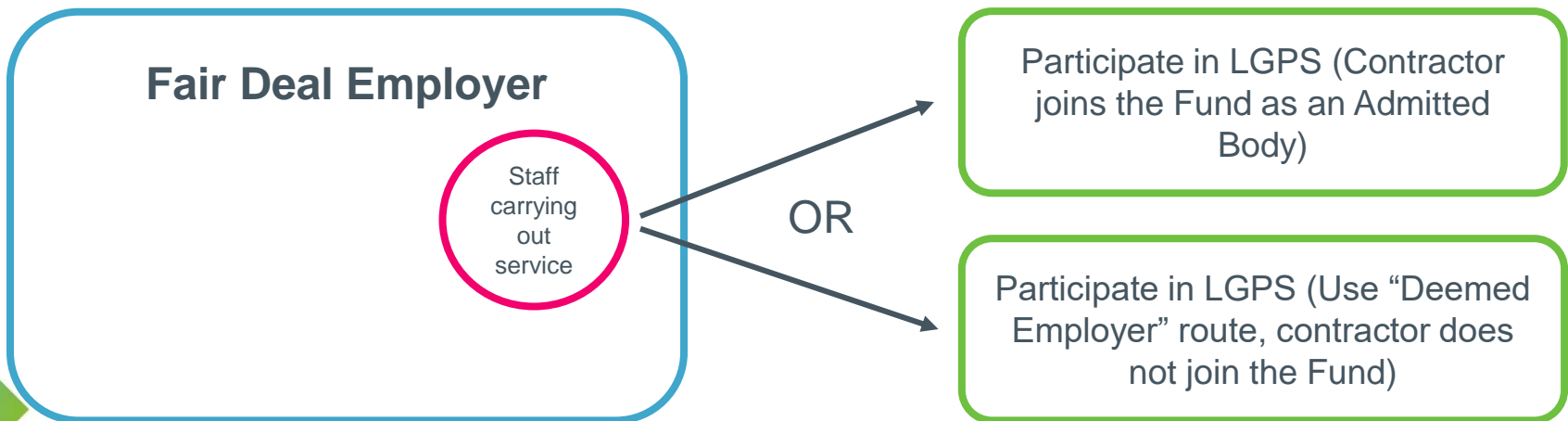
Consultation closed 31 July 2019

New Fair Deal consultation

Current approach – Best Value Directions 2007

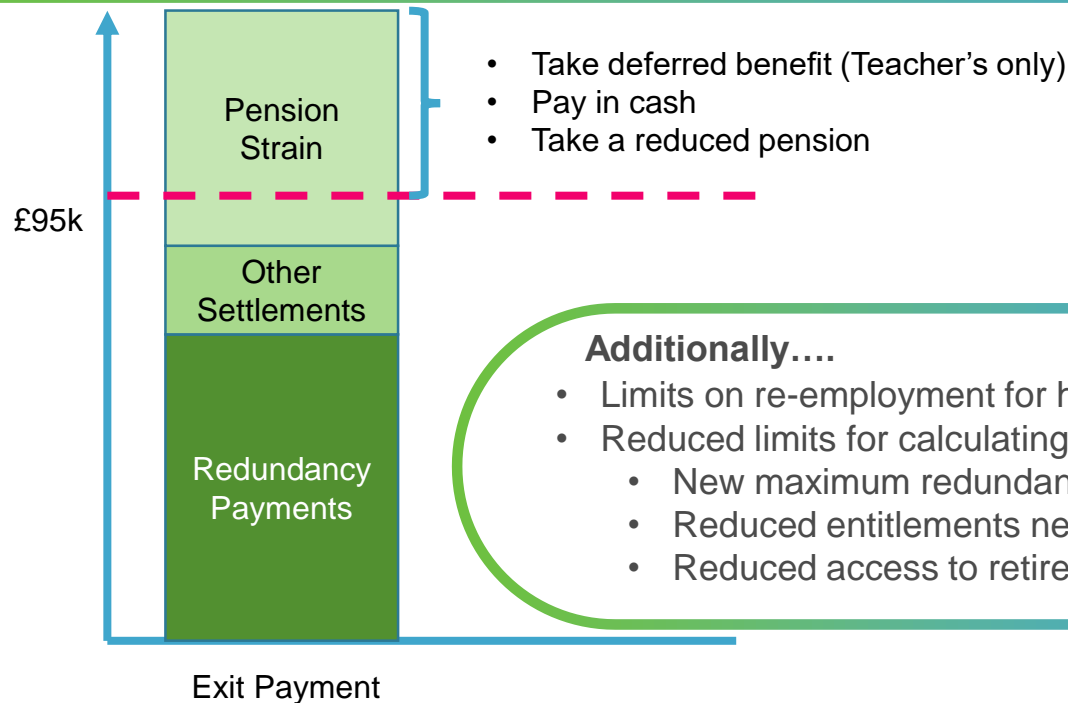


Proposed approach – Fair Deal in the LGPS



Public Sector Exit Payment Cap

- Total exit payments to an individual should not exceed £95k
- If they do the employer must **reduce** any of the elements that make up the exit payment so as not to exceed £95k
- The exit payment cannot be reduced below any statutory redundancy payment



Additionally....

- Limits on re-employment for high earners
- Reduced limits for calculating exit payments:
 - New maximum redundancy settlements
 - Reduced entitlements near retirement
 - Reduced access to retirement options

Potential impact on LGPS

Examples of roles & real voluntary redundancy schemes:

CAPPED
Trading Standard
Manager
£44k 20 years

CAPPED
Adult Social Care Worker
£35k 30 years

CAPPED
HR staff
£28k 40 years

CAPPED
Planning Manager
£51k 15 years

Consultation closed 2 July 2019, awaiting outcomes

Good Governance in the LGPS



Good governance in the LGPS

Phase II report from Working Groups to SAB

November 2019

Conclusions

- Outcomes based model instead of prescribed approach
 - Robust management of conflicts of interest
 - Policy on member and employer representation
 - Level of knowledge and understanding
 - KPIs to measure level of service to fund stakeholders
 - Sufficient resources to effectively manage and administer the fund
 - Independent review of a fund's governance
- Independent review of a fund's governance arrangements
- Improvement plans where needed

Next steps

- Drafting proposed changes to Guidance
- Establish KPIs to measure service standards
- Define contents of Governance Compliance Statement

PLSA retirement income targets

- The Pensions and Lifetime Savings Association (“PLSA”) announced new retirement income targets in October
- The targets indicate the level of annual expenditure required to achieve a minimum, moderate and comfortable standard of living in retirement



Translating the targets into “real life”

	Minimum	Moderate	Comfortable
Single	£10,200 a year	£20,200 a year	£33,000 a year
What standard of living could you have?	Covers all your needs, with some left over for fun	More financial security and flexibility	More financial freedom and some luxuries
House	DIY maintenance and decorating one room a year.	Some help with maintenance and decorating each year.	Replace kitchen and bathroom every 10/15 years.
Food & Drink	A £38 weekly food shop.	A £46 weekly food shop.	A £56 weekly food shop.
Transport	No car.	3-year old car replaced every 10 years.	2-year old car replaced every five years.
Holidays & Leisure	A week and a long weekend in the UK every year.	2 weeks in Europe and a long weekend in the UK every year.	3 weeks in Europe every year.
Clothing & Personal	£460 for clothing and footwear each year.	£750 for clothing and footwear each year.	£1,000 - £1,500 for clothing and footwear each year.
Helping Others	£10 for each birthday present.	£30 for each birthday present.	£50 for each birthday present

Thank you



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