

## **PENSIONS COMMITTEE – 8 FEBRUARY 2005**

### **PENSION FUND - ACTUARIAL VALUATION**

#### **SUMMARY**

This report notes that the Actuary's report on the triennial actuarial valuation of the Council's pension fund was received at the end of January and summarises the outcome of the valuation. It also proposes a Funding Strategy Statement for adoption, and suggests that an asset/liability study be carried out following on from the actuarial valuation.

#### **RECOMMENDATIONS - That**

- (1) The report of the Actuary on the valuation of the Pension Fund as at 31 March 2004 be agreed, subject to the Council agreeing the increase in Bexley Council's employer contributions from 1 April and amending the Council's financial plans accordingly;
- (2) The Funding Strategy Statement be approved; and
- (3) An asset/liability study be carried out by Mercer Investment Consulting with the cost met by the Pension Fund.

#### **1. Introduction**

The Council is required to have an actuarial review of its pension fund every three years and this Committee has delegated powers to agree the subsequent report of the actuary. However, where the impact on the Council's budget exceeds £1m the financial implications must be agreed by full Council. The Council's Actuary, Mercer Human Resource Consulting, has now completed the valuation and the report is attached. The report has to be agreed by the Council by 31 March 2005 and implemented from 1 April 2005.

Three copies of the Actuary's report have been placed in the Members' Room.

This report gives further details of the outcome of the valuation and considers associated matters. A detailed briefing has previously been provided to representatives of the Committee.

#### **2. Valuation Method and Assumptions**

The objective of the valuation is to ensure that the assets of the fund are sufficient to cover existing and future liabilities. Any shortfall is met by an increase in the employers' contributions from the Council and the other admitted bodies.

The valuation method used is the same as in the previous valuation. It assesses the extent to which current service liabilities have been funded and secondly assesses the cost of future service liabilities. Assets have been assessed at market value.

The key assumptions for future service are:-

- Price inflation 2.5%
- Pay inflation 4.25%
- Investment returns 6.5%

The Actuary has assumed that the fund's overall assets will outperform the return from investing solely in risk free investments such as government bonds by 1.5% reflecting the proportion of funds invested in equities. However it is suggested that the investment strategy should be reviewed regularly having regard to the liabilities of the fund. This issue is addressed in section 6 below.

On demographic assumptions the Actuary has largely retained the assumptions used previously, but has made two key changes:-

- extra allowance for increased life expectancy of members.
- reduced allowance for ill health retirements, based on actual experience in Bexley over recent years.

### 3. The Results of the Valuation

Fund membership has increased over the last three years and is summarised below.

	31 March 2001	31 March 2004
Employees	4,327	4,284
Pensioners	2,858	3,131
Former Employees	2,157	2,955
<b>TOTAL</b>	<b>9,342</b>	<b>10,370</b>

The number of employees in the fund has remained steady as has the average age of current employees in the fund. This is important as a rise would imply additional long term costs.

The market value of the fund stood at £297.4m at 31 March 2004 compared to £314.4m at the time of the last valuation. In terms of existing liabilities the fund has a deficit of £60.4m as at 31 March 2004 and the overall funding level stands at 83% (compared to 104% previously). This reduction was anticipated in the interim review of the Fund reported to this Committee last year. Recent analysis by CIPFA suggests that on average local government schemes are now only 74% funded.

The Actuary considers that, for Bexley employees, the long-term contribution rate would be 11.1% (this compares to 12.7% three years ago and is largely due to the increase in working life assumed following the changes to regulations from April 2005 –

see report on Scheme changes elsewhere on this agenda). However, the deficit on the Fund requires a further contribution of 6.1% a year to recover the shortfall over a period of 20 years. This results in a total contribution rate of 17.2%. If this were implemented immediately it would add around £3m a year to the current contribution rate of 11%. The Actuary considers it reasonable to phase in this rate over six years - two valuation periods.

The recommended levels of contributions over the three years covered by the actuarial report are, therefore:-

<u>Employer</u>	<u>2005/06</u>	<u>2006/07</u>	<u>2007/08</u>
Bexley Council	12.5%	14.0%	15.5%

Subject to the results of subsequent valuations, the level of employer's contributions would ultimately rise to around 17.2%.

#### **4. Funding Strategy Statement**

The Council is required to draw up and publish a Funding Strategy Statement for the scheme by 1 April 2005, as suggested by the draft regulations reported to this Committee in December 2003. This document is considered by the Actuary as part of the valuation process, and acts as a bridge between the Statement of Investment Principles and the valuation. A draft of the document has been consulted with the Actuary during the valuation, and with admitted and scheduled bodies over the last few months. A final draft, including comments received, is now attached for this Committee's approval.

#### **5. Impact on Other Employers**

The contributions and phasing for other employers participating in Bexley's Pension Fund recommended by the Actuary are shown in the Appendix.

These bodies have been consulted on a draft of the Actuary's report and discussions held with them about implementing their new contribution rates so that they could take account of the changes in their budgetary processes. Copies of the Actuary's final report and certificates will also be sent to them.

#### **6. Asset/Liability Study**

Following the last actuarial valuation in 2001 the Council commissioned an asset/liability study. This resulted in the creation of a scheme specific benchmark against which to measure fund performance, and a change in the asset allocation from a 70/30 equity/bond split to 60/40. Following the completion of the valuation, it is now an opportune time to undertake a further study.

The study will review the asset allocation of the Fund in the context of its long term liabilities.

The cost of a study from Mercer Investment Consulting is estimated at between £24,000 and £27,000. On balance it is suggested that it would be useful to

commission an asset liability study now to update debate on investment policy. A report on the outcome should be ready for the next meeting of the Committee.

## **7. Summary of Financial Implications**

Each 1% increase in the employer's contribution rate for the Council is estimated to cost some £500,000 a year. A 1.5% increase each year from April 2005 onwards will therefore add £750,000 a year to the Council's costs.

The effect of the reduction in the employer's rate for MCCH Society Ltd in 2005/06 is a saving of some £60,000, and this should be reflected in a reduced Council contribution to the Learning Disabilities Pooled Budget. The cost of meeting the increasing rates for Care Partners Trust and KCHT will be the subject of negotiation with the organisations concerned, but could add up to £75,000 a year to the Council's budget for each of the next three years, whilst the reduction in Bexley Care Trust's contributions should reduce the Council contribution to the budget by £12,000 in 2005/06. The reduced cost to Bexley Heritage Trust of around £9,000 will be reflected in the grant awarded for 2005/06. Other changes in employers' contributions have no direct effect on the Council and there is no impact on employee contributions.

The net impact on the Council of the changes to the admitted bodies' employer contributions is, therefore, likely to be a small saving in 2005/06, but a net cost of around £75,000 in each of the following two years.

The budgetary impact of the revised phasing of contributions will, subject to Council approval, be included in the Council's Budget and Corporate Policy and Resource Plan.

The cost of the asset/liability study would be met directly by the Pension Fund.

### **Local Government Act 1972 – section 100d**

#### **List of background documents**

Bexley London Borough Pension Fund – Actuarial Valuation as at 31 March 2004 – Mercer Human Resource Consulting – January 2005.

**Contact Officer:** Nigel Bate, Head of Technical Finance. Extn 2647

**Reporting to:** David Berry, Director of Finance and Business Services

APPENDIX

EMPLOYERS' CONTRIBUTION RATES from 1 APRIL 2005

	<u>Employer's Contribution Rate (%)</u>			
	<u>Existing</u>	<u>2005/06</u>	<u>2006/07</u>	<u>2007/08</u>
<u>Scheduled Bodies</u>				
Bexley College	11.5	12.2	12.2	12.2
<u>Admitted Bodies</u>				
Rose Bruford College	14.5	15.5	15.5	15.5
MCCH Society Limited	15.5	12.4	12.4	12.4
London and Quadrant Housing Trust	11.0	16.0	21.0	26.0
Orbit Housing Association	16.9	18.9*	18.9*	18.9*
Kent Community Housing Trust	17.5	19.9	22.3	24.7
Bexley Heritage Trust	13.9	8.9	8.9	8.9
Danson Youth Trust	13.0	16.2	16.2	16.2
Care Partners Trust	17.5	19.3	21.1	22.9
Business Academy Bexley	11.0	9.6	9.6	9.6
Business Academy Bexley (Primary)	-	9.7	9.7	9.7
Bexley Primary Care Trust	14.0	12.3	12.3	12.3

\* Orbit will also have to pay a lump sum contribution each year to meet their deficit in place of a higher percentage contribution on their remaining 4 admitted staff.