CT/20/15
Devon Pension Board
16th January 2020

ACTUARIAL VALUATION 2019

Report of the County Treasurer

Please note that the following recommendations are subject to consideration and determination by the Committee before taking effect.

Recommendations: **that the Board notes the approach and progress of the 2019 triennial valuation of the Pension Fund.**

1. Introduction

1.1. Every three years Devon County Council (as the administering authority) is required to have an actuarial valuation of the Devon Pension Fund conducted by a qualified independent actuary. Barnett Waddingham are the Council's appointed Fund Actuaries.

1.2. The purpose of the valuation is to establish the Fund's liabilities in relation to its assets and determine the current funding level, and to set contribution rates for the Fund's employers for the next three years. The approach to the Valuation has to take into account Section 13 of the Public Sector Pensions Act 2013.

1.3. The Actuary met with officers in September to confirm the assumptions to be used for the valuation. The Actuary has now provided the Fund level results from the Valuation and this is summarised in this report. Melanie Durrant and Louise Lau from Barnett Waddingham attended and presented the results to the Committee and also the employers meeting in November.

2. Factors taken into consideration

2.1. The triennial actuarial valuation examines how the assumptions built into the previous valuation have fared and then considers future prospects for the Fund. The Actuary has to certify levels of contribution to secure the solvency of the Devon Fund, but also have regard to the desirability of maintaining as stable a contribution rate as possible.

2.2. The Actuary also has to take into account Section 13 of the Public Sector Pensions Act 2013. This provides for an independent review (by the Government Actuary's Department (GAD)) of the valuation and employer contribution rates to check that they are appropriate and requires remedial action to be taken where that review identifies a problem. The Actuary will therefore aim to ensure that the assumptions applied will lead to contribution rates that ensure the long term cost efficiency of the fund and achieve solvency over an appropriate period, and thereby seek to avoid any red flags when GAD carry out their review. Long term cost efficiency is now seen as a requirement while stability of contribution rates is only "desirable".

2.3. The following factors, outlined in paragraphs 2.4 to 2.6, have been considered by the Actuary and have been taken into account in the current valuation, and calculation of the level of deficit and future contribution levels.

2.4. ***Inter-valuation experience*** – The valuation will be impacted by what has happened over the three years since the last valuation, compared to the assumptions made by the actuary at the time. The experience of pay and pension increases and mortality rates against the assumptions made in 2016 have been marginal. However, investment returns have been above the expected level, 9.1% per year against the actuarial assumption of 5.5%, and this has had a positive effect in reducing the deficit position.

2.5. ***Revised assumptions*** – These include:

(a) Price Inflation – based on the Bank of England's 20 year inflation curve, average CPI estimated at 2.6% in projecting future liabilities. This compares with an estimate for CPI of 2.4% at the 2016 Valuation.

(b) Salary Increases – Assumed to be equivalent to CPI until 31 March 2020, and 3.9% thereafter. The level of pay increases takes into account the effect of increments and promotions for individual members of the Fund, not just the national pay awards.

(c) Statistical Assumptions – The key factor influencing pension liabilities is pensioner mortality, i.e. how long pensioners will be receiving their pension. The Actuary uses national statistical tables and then adjusts them based on an analysis of the Devon Pension Fund's membership. Improvements in longevity have slowed down at a national level, and this has resulted in reduced longevity assumptions, and therefore a reduced impact on the Fund's liabilities.

(d) Discount Rates – In determining the value of accrued liabilities and future contribution requirements it is necessary to discount future payments to and from the Fund. Barnett Waddingham's approach is to reflect the investment return expected to be achieved from the underlying investment strategy. The investment return going forward has been assumed to be 5.1%, which compares with an assumption of 5.5% at the last valuation. This is summarised in the following table:

Actuarial Valuation 2016 - Breakdown of Discount Rate

Asset Class	Percentage of Fund	Assumed Return	Real (relative to CPI)
Equities	58%	6.7%	4.1%
Bonds	15%	2.6%	0.0%
Property and Infrastructure	18%	6.1%	3.5%
Cash	1%	0.8%	-1.8%
Diversified Growth Funds	8%	4.8%	2.2%
Expenses (deduction)		-0.2%	
Neutral estimate of discount rate based on long-term investment strategy		**5.6%**	**3.0%**
Prudence allowance		-0.5%	
Discount rate assumption		**5.1%**	**2.5%**

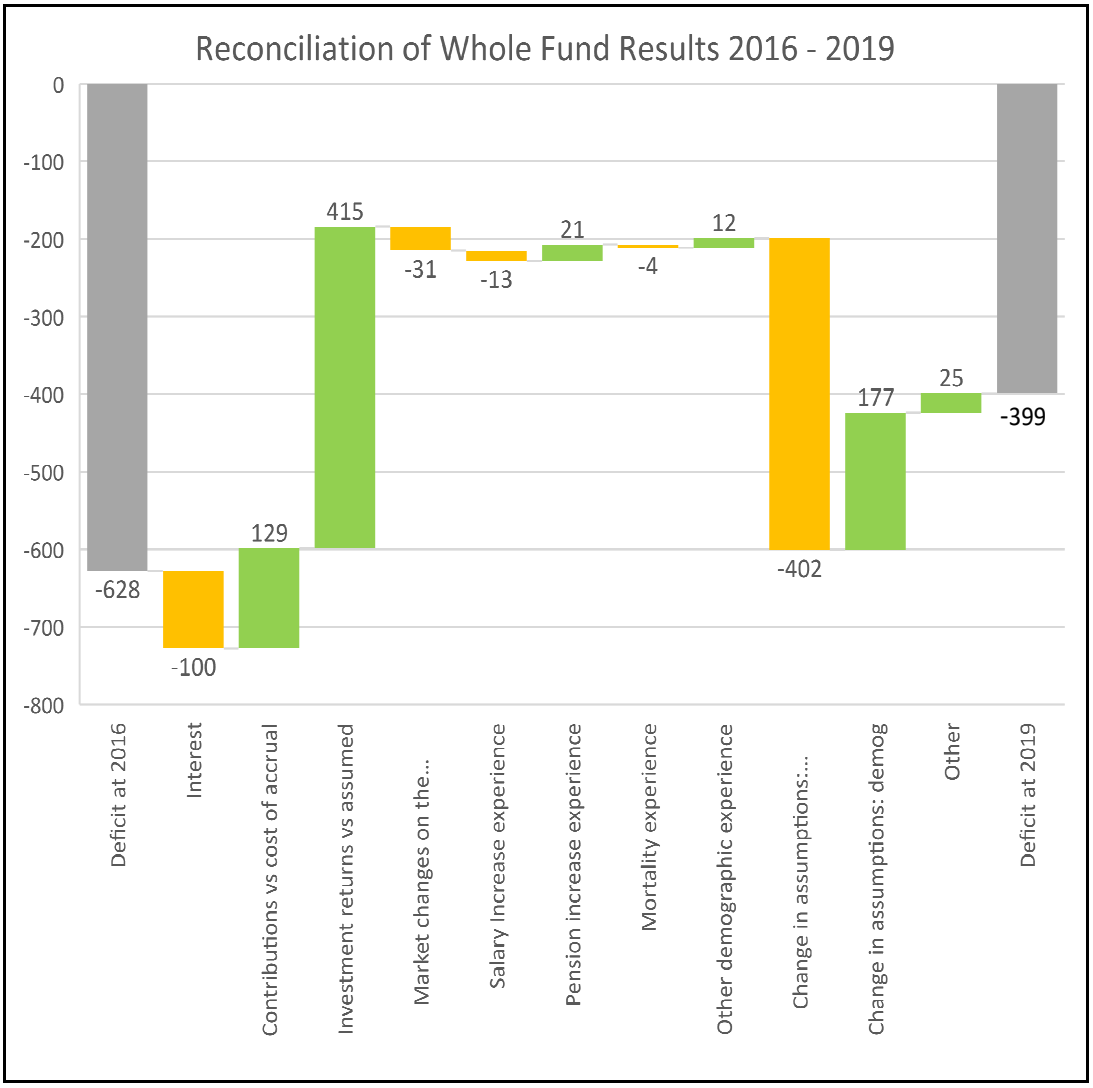
2.6. ***Deficit recovery period*** – At the last valuation the length of the recovery period was reduced from 25 to 22 years. At this valuation the Actuary has reduced the average recovery period to 19 years. There is some logic to this, in that the ultimate aim is to reach 100% funding, and as we are three years further on since the last valuation, a reduction of three years in the recovery period demonstrates that the Fund is progressing towards that goal. Reducing the recovery period will decrease the level of risk to the Fund and reduce the cost of meeting the deficit.

3. Overall results

3.1. The Actuary has determined that the Devon Fund has a funding level of 91%, up from 84% at the 2016 Valuation. The Fund's assets were valued at £4,273m against future pension liabilities assessed at £4,672m, giving a deficit for this valuation of £399m. This, along with the comparative figures for the previous valuation in 2016, is shown in the table below:

	2016 Results	***2019 Results***
Assets	£3,311m	£4,273m
Liabilities	£3,939m	£4,672m
Deficit	(£628m)	(£399m)
Funding Level (whole Fund)	84%	91%

3.2. The following table shows a reconciliation of the deficit as at 31 March 2016 with the deficit as at 31 March 2019:



3.3. The change in financial assumptions, i.e. the reduction in the discount rate, will result in higher primary rate contributions for employers. The primary rate is the rate payable for the additional pension liabilities accrued during the year. The average primary rate for employers will increase from 14.9% to 16.9% of pensionable pay. However the improved funding level will result in lower deficit contributions being required, which will offset the increased primary rate. This is summarised in the table below:

	2016 Results	***2019 Results***
Primary Rate	14.9%	16.9%
Deficit Contributions	£36.3m	£22.2m
Total Projected Contributions as % of Payroll	20.9%	20.5%

4. Effects on Individual Employers

4.1. The valuation results presented in this report represent the average for the Fund. The position of each employer will be different, based on the profile of their fund members and cashflows in and out of the Fund. As a result, some fund employers will see their overall contribution rates, including deficit payments, reduce, while others will see increases. However, the Actuary will aim to maintain stable contribution rates where possible. As in previous years deficit contributions will be quoted as cash amounts rather than as a percentage of pensionable pay.

4.2. In order to achieve as stable a rate as possible, groups of smaller employers have been put together in pools to even out their contribution rates. This reduces the level of volatility in their contributions. At the 2016 Valuation academies were pooled by Local Education Authority (LEA) area. However, as many multi-academy trusts now cross LEA boundaries, it is proposed to put all academy employers into a single pool.

4.3. It is recognised that where there are contribution increases, this will place extra pressure on employers following the long period of austerity, but as outlined in paragraph 2.2 above the Fund needs to ensure that sufficient contributions are being paid to ensure long term cost efficiency and achieve full funding over an appropriate period. This is a requirement of Section 13 of the Public Sector Pensions Act 2013, and will be reviewed by the Government Actuary's Department once the Valuation is complete.

4.4. In order to assist employers seeking to reduce their costs some LGPS funds give a discount to employers who pay their contributions early. Where contributions are paid early, this provides the opportunity to invest them at an earlier stage and therefore provide a return to offset the impact on the Fund of the discount given. This can work well when the fund enjoys a positive return, but can be a risk if the contributions are paid just before a period of negative returns. That risk would fall upon the employer paying their contributions early, rather than on the Fund as a whole.

4.5. Assuming that the forecast investment return equates to the discount rate used by the Actuary in undertaking the Valuation, then the appropriate discount would be half the discount rate. However, some further allowance should also be made for prudence, recognising the risk to achieving the forecast investment return. It is therefore been agreed to allow employers a 1.5% discount on early payment of their set deficit contributions, where they are set cash amounts, on the proviso that the payment is received on or before the date on which their April contributions are paid. No discount would be applied to primary rate contributions. If an employer wishes to pay three years of deficit contributions in advance, then a discount of 4.5% will be applied.

5. Conclusion

5.1. The 2019 Valuation demonstrates that the Fund is making progress towards the long term objective of 100% solvency, with the funding level increasing from 84% to 91%, and the deficit recovery period reducing from 22 to 19 years. The reduction in the average recovery period will help to reduce the cost of pensions in the longer term.

5.2. The vast majority of fund employers were notified of their new employer rates by the end of December save for a handful of admitted bodies and some post 2019 new academies which are outstanding. The formal certification of the rates will not be until the end of March, in order to take into account any issues that are identified in the intervening period. However, it is unlikely that the results will change significantly from the provisional results.

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Electoral Divisions: All
Local Government Act 1972
List of Background Papers - Nil
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