Executive

LGPS Pension Scheme Update

12 April 2010

Report of the Head of Finance and the Head of Human Resources

PURPOSE OF REPORT

This report sets out an overview of the current position on the funding of the pension scheme, the potential implications arising from the triennial review of the pension fund and a review of local discretions on the scheme.

This report is public

Recommendations

The Executive is recommended to:

(1) Note the contents of the report.

(2) Ask officers to provide an analysis of the financing options available to the Council once the 2010 valuation is finalised including the impact on the Medium Term Financial Strategy.

(3) Approve the changes to local pension discretions as detailed in Appendix 1.

Executive Summary

Background

1.1 The Local Government Pension Scheme (LGPS) was in deficit at the 2007 valuation and the impact on Cherwell was a deficit of £31m. On the basis of this valuation the employer's pension contribution was increased by 1% to 21.7%. This increase was meant to cover the deficit of the duration of the life of the scheme. At the same time employee contributions also changed and were based on salary bands. The current rates paid are between 5.5% and 7.5% depending on salary earned. In 2009/10 the Council will make payments of £2.477m into the fund and current employees will pay £0.742m.

1.2 The estimated position prepared for the financial statements by the actuary at March 2009 (FRS17 Report) indicated a further increase to the deficit at a total of £42m. Whilst the majority of this increase may be due to the economic situation and turbulence in the financial markets it is expected that employer contributions will have to increase as a result of the 2010 valuation at 31st March 2010. At present our Medium Term Financial Strategy assumption is based on an increase of 3.1%.

1.3 The Department for Communities and Local Government (CLG) issued an informal consultation paper in 2009 entitled Local Government Pension Scheme – Delivering Affordability, Viability and Fairness. The key elements proposed in this consultation are:

a) a change to the solvency requirements from 100% funding target to a lower figure which would still need to take full account of the affordability of employers liabilities to pay pensions and to meet liabilities when undertaking three yearly fund actuarial valuations. This will still need to ensure that liabilities can be met as they fall due.

b) the creation of a more ‘flexible funding model’ to reduce the potentially unrealistic burden imposed by current requirements on scheme employers and, potentially Council Tax payers.

c) the retention of the existing scheme regime, but with the additional ability of the locally administering scheme to set a funding target that does not necessarily need to be set at 100%. This would in effect retain the long term requirement for 100% funding but allow greater flexibility to administering authorities.

d) A revised contribution tariff which, subject to consultation could take effect from 1 April 2010. This element has not been changed and the contribution rates by salary band remain at the same rates as 2009/10 and can be seen in Appendix 1.

1.4 The Council`s pension fund is administered by Oxfordshire County Council. Oxfordshire County Council is the administering authority for the Oxfordshire Pension Fund. Over 50 employers and their staff contribute to the fund. The county council is responsible for maintaining, administering and paying out all benefits from the pension fund.

1.5 The County provide an annual audited financial report to officers that provide a useful indicator on the financial position of the fund.

1.6 The Pension Fund Committee is responsible for the pension fund's investment arrangements. This committee is made up of elected council members advised by the Head of Finance and Procurement at Oxford County and an independent financial advisor.

1.7 A beneficiary’s observer also attends the committee meetings. The observer is allowed to participate in discussions but has no voting powers. The observer sends reports to all 50 employers for a wider distribution.

1.8 The Pension Fund Committee meets quarterly to review fund progress. Cherwell District Council has the opportunity to attend these meetings and receive all agendas and reports.

1.9 The pension fund committee has recently consulted with all members of the scheme on the CLG consultation and at its meeting on 19th March 2010 has made recommendations to amend the funding strategy statement. These amendments are extracted from paragraph 14 of "the Pension Fund Committee Report Agenda Item 15 – the Funding Strategy Statement":

Having considered the various responses to the consultation letter, it is proposed to vary the current Funding Strategy Statement as follows:

- Recovery Period. The mixed response to the consultation question appeared to hide a reasonable consensus that whilst it is not appropriate to spread today's real costs too far into the future, the ability to smooth contribution rates by extending the recovery period to cope with increased past service deficits caused by the poor performance of the markets at the time of the Valuation is to be welcomed. Such smoothing will avoid future volatility in contribution rates where future valuations are undertaken at more normal market levels or indeed at market highs where past service deficits are artificially reduced by unsustainable asset valuations. In this latter case it may well be appropriate to shorten recovery periods to avoid a short term and unsustainable reduction in employer contribution rates. It is hoped that there are sufficient flexibilities open to the Actuary to smooth the majority of variations in contribution rates resulting from short term movements in the financial markets. It is expected therefore that under most Valuations, the recovery period will be set at a maximum of 25 years. However it does seem sensible to leave the option to extend recovery periods in extreme cases to avoid a short term increase in contribution rates, to be reduced again when markets recover. It is therefore proposed to amend the Funding Strategy Statement to allow a variation in the recovery period, consistent with the need to maintain stability in the overall employer contribution rate in light of short term market fluctuations. It should be noted that under this amendment, the recovery period would not be extended to reduce increases in contribution rates which are deemed to be more permanent in nature, e.g. those stemming from an increase in longevity assumptions, or from a downward trend in pensionable payroll. It should be further noted that the Administering Authority retains the discretion as to the actual recovery period used in each valuation, and is not required to accept the request from any employer for any particular recovery period.

- Stepping Allowances – As with the extension of the recovery period, there is general support for the use of a six step approach to increasing contribution rates as a means of maintaining as near stable contribution rate as possible. The Administering Authority again retains the right as to when to exercise the discretion to allow an employer to step an increase over 6 years. In these circumstances it is proposed to amend the Funding Strategy Statement to widen the definition of exceptional circumstances under which 6 steps are allowed, to include exceptional financial hardship.

- Definition of Solvency – In light of the clear consultation response, it is recommended to retain the current definition of solvency as 100% of total liabilities, and no amendment is proposed to the Funding Strategy Statement on this matter.

- Investment Strategy – In light of the responses to the consultation, and the absence of any clear response for immediate access to a low risk investment strategy, it is proposed that this issue is not taken forward at this time. It is therefore not proposed to make any changes to the Funding Strategy Statement in respect of this issue.

- Approach to Community Admission Bodies – The strong consensus from the consultation exercise is to move to a single approach to valuation for all scheme employers, irrespective of whether their membership of the Fund is through an admission agreement, or set out directly in the Regulations. It is therefore proposed that the Funding Strategy Statement should be amended to remove those aspects which have provided a distinction in approach between admitted bodies and others, so that future valuations are undertaken on a single set of valuation assumptions.

1.10 These amendments will be factored into the impact of the impending pension fund triennial valuation.

Pension Fund Triennial Valuation

1.11 The pension fund is administered by Oxford County Council. And a formal actuarial valuation is carried out once every three years.

1.12 The position of the actuarial valuation as at March 2007 showed a deficit of liabilities over assets of £31 million. The pension fund deficit at that time required the Council to increase its contribution rate by an additional 1% above the increases resulting from the 2004 valuation from 20.7% of staff pay in 2007/08 up to 21.7% from 2008/09. The council took the decision to increase the contribution rate by this additional 1% in full in the 2008/09 budget. The actuary calculated that this increased contribution rate of 21.7% for a sustained period of time would make good the deficit.

1.13 The impending actuarial valuation in March 2010 will set the employers contribution rates for the following 3 year period. Given the recent economic conditions, it is anticipated that the contribution rates will need to increase substantially. The proposals from CLG are an attempt to mitigate the otherwise likely rise in pension contributions that may occur.

1.14 The Council has taken into consideration the March 2010 valuation when making decisions relating to the size of the organisation in relation to the expressions of interest exercise and the outsourcing of the back office processes of the revenues and benefits functions.

1.15 One element of the valuation will be based on the number of current employees as at 31 March 2010. As a result the Council has approved many of the expressions of interest prior to this date so this will reduce number of employees by 9 and the outsourced contract which was due to commence on 1 April 2010 was bought forward to February 2010 and this reduced employees by 19.

1.16 The Council has also reviewed how timely information is shared with the County regarding the profile of the Council to ensure that the most up-to-date information is used in the valuation.

1.17 If the actuarial valuation follows the current scheme requirements, it is likely that the Council will bear a significant additional financial contribution from 2011/12. Whilst this is an unknown, an allowance has been made in the Medium Term Financial Strategy and this will be reviewed as soon as further information is available.

1.18 The Council may decide to make a one-off capital payment into the pension fund to reduce their share of the deficit and minimise the impact on the annual revenue budget of increased employer contributions. This would mean that the Council would forego the use of these funds for future capital schemes and until use investment income. However the cost benefit analysis of making a one off payment and reducing annual pension costs may be attractive financially in the longer term. Each 1% increase in the pension fund would equate to approx £120,000.

1.19 The Council would need to consider the impact of making this one off payment on Council priorities and need to work with the County and pension actuary to understand the benefits of this additional one off payment and consider the cost benefit analysis to the Council.

1.20 It is recommended that Officers consider a one off payment and prepare a further report for members once the results of the valuation are known. This is anticipated in October 2010 in time for the budget 2011/12 cycle to commence. This can then be evaluated together with the Council`s priorities for 2011 onwards.

Pension Fund Local Discretions Policy

1.21 The pension regulations require the Council to formulate, publish and keep under review its policies in respect of certain areas of the Scheme where it may exercise its discretion. Following the introduction of the new LGPS on 1 April 2008, some of the previous discretions have disappeared whilst new ones have emerged and it would seem an opportune time to review this issue.

1.22 Such discretionary provisions in the LGPS enable local authority employers to manage employment situations to the advantage of the Council and the employee, although any such associated costs need to be taken into consideration during any decision making process. This is especially important at a time when local authorities need to be flexible and ensure a degree of organisational change can be implemented. This is likely to impact on the numbers and type of staff required in the future. This discretionary pension's policy will facilitate the achievement of any changes in a way that supports those that are directly affected and hopefully will remain sufficiently attractive to attract those that wish to take voluntary redundancy as well as supporting good employee relations.

1.23 Reviews of this policy under these regulations can only take place on an annual basis and once agreed must not be implemented until at least one month has passed from the date of publication. Therefore it is proposed any changes take place with effect from 12 May 2010 (one month after the appropriate Executive meeting).

1.24 The full list of discretions highlighting any amendments is attached as Appendix 1 including those relating to the administering body. Many of these discretions cover events which are only likely to occur very infrequently.

Conclusion

1.25 The pension fund triennial valuation is due to be conducted as at March 2010. The likelihood is that this will require an increased employer's contribution rate, which the Council will need to fund. As a result the Council will give consideration to a potential one off capital payment into the fund and will ask Officers to consult with the County and pension fund actuary to prepare an analysis for further consultation in October 2010.

1.26 An informal consultation paper from the department of Communities and Local Government has suggested some scheme changes that may affect the valuation process and the employee and employer contribution rate. The Oxfordshire Pension Fund Committee has considered this consultation and has made some amendments to the financing strategy of the scheme ahead of the valuation.

1.27 The pension regulations require the Council to formulate, publish and keep under review its policies in respect of certain areas of the pension scheme where it may exercise its local discretion. This review has been carried out and detailed in Appendix 1.

Consultations

The CLG consultation paper has been discussed with all members of the Oxfordshire County Council LGPS scheme and the Pension Fund Committee has considered these consultations when making recommendations regarding the funding strategy statement for the scheme.

Implications

Financial:	Financial Effects: There are no financial effects on the Council as a result of this report although the impact of the pension fund valuation will have financial implications in relation to contribution rates. At present the Medium Term Financial Strategy has made assumptions and these will be reviewed in line with new information from the valuation and consideration of a one off capital payment into the scheme. Any local pension discretions offered may have a financial implication and these would be considered in all individual business cases before a decision is made. Comments checked by Karen Muir, Corporate Accountant, 01295 221559.
Legal:	There are no legal effects of this report. Comments checked by Liz Howlett, Head of Legal and Democratic Services/Monitoring Officer 01295 221686
Risk Management:	The LGPS must be sustainable over the long term and funding of the scheme needs to be included in the medium term financial forecast. If the Council fails to consider the impact of the pension deficit and increased contributions then they will fail to deliver a balanced budget. The MTFS makes assumptions regarding pension

rates and officers are considering proposals to reduce the carrying value of the pension deficit and minimise the impact on annual contributions by making a one off capital payment into the scheme.

Comments checked by Karen Muir, Corporate Accountant, 01295 221559.

Wards Affected

All

Corporate Plan Themes

An Accessible, Value for Money Council

Executive Portfolio

Councillor James Macnamara - Portfolio Holder for Resources and Organisational Development

Document Information

Appendix No	Title
Appendix 1	Local Pension Discretions 2010/11
Background Papers	
FRS 17 Data – March 2009 Medium Term Financial Strategy Pension Fund Committee Agenda`s – Dec 4 2009 and March 19 2010 LGPS (Administration) Regulations 2008 LGPS (Benefits, Membership and Contributions) Regulations 2007 LGPS (Transitional Provisions) Regulations 2008.	
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