Report To:	**Pension Fund Management/Advisory Panel**
Date:	23 September 2016
Reporting Officer:	Sandra Stewart, Executive Director of Governance, Resources and Pensions Euan Miller, Assistant Executive Director, Funding and Business Development
Subject:	**SECTION 13 VALUATION**
Report Summary:	This report provides a summary of the Section 13 valuation which will be undertaken by the Government Actuary's Department (GAD) as part of the 2016 actuarial valuation process for LGPS funds in England and Wales. The report also provides a summary of the 'dry-run' that GAD has undertaken using the 2013 LGPS valuations.
Recommendations:	Members are recommended to note the report.
Policy Implications:	None.
Financial Implications: **(Authorised by the Section 151 Officer)**	Employer contribution rates in the LGPS are determined by the triennial actuarial valuation process. The latest actuarial valuation is currently ongoing, with an effective date of 31 March 2016. The Section 13 valuation has no direct impact on contribution rates, but its existence may help ensure that all funds set contributions at an appropriate level.
Legal Implications: **(Authorised by the Solicitor to the Fund)**	It is a statutory requirement for an actuarial valuation of the Fund to be undertaken every three years. The work carried out must comply with the relevant regulations and professional standards. The Section 13 valuation process helps ensure that this is the case.
Risk Management:	A key risk when administering the LGPS is that an employer fails whilst its sub fund is in deficit. The valuation adjusts employer contribution rates with the aim of matching asset and employer values in the future, in line with the GMPF's Funding Strategy Statement.
Access to Information:	**NON-CONFIDENTIAL** **This report does not contain information which warrants its consideration in the absence of the Press or members of the public.**
Background Papers:	The background papers relating to this report can be inspected by contacting Euan Miller, Assistant Executive Director – Funding and Business Development.

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1 BACKGROUND

1.1 The 2016 LGPS valuations in England and Wales will be the first to be reviewed under the new framework set out in Section 13 of the Public Service Pensions Act ("S13"). This piece of primary legislation requires that an appointed person, in this case, the Government Actuary's Department ("GAD"), reports on whether each LGPS fund's formal funding valuation adheres to the following criteria.

Compliance – to confirm the valuation has been carried out in accordance with the LGPS Regulations

Consistency – to confirm the valuation is not inconsistent with other LGPS funds' valuations and that differences in assumption and methodology can be justified and evidenced

Solvency – to confirm contributions are sufficient to ensure solvency

Long term cost efficiency – to confirm contributions are sufficient to meet benefit accrual and repay any existing deficit

1.2 If GAD has concerns about LGPS funds under any of these measures then they can recommend remedial actions (such as imposing a given level of contributions on employers in the fund) which may ultimately be enforced by DCLG using powers granted under the legislation.

2. APPROACH

2.1 In summary, GAD will calculate a number of metrics for each of the LGPS funds using consistent actuarial assumptions. Funds will be ranked in a league table based on these metrics and assigned a RAG (Red/Amber/Green) status against each metric to identify those funds that may need to take action. The absolute value of the assumptions in the chosen actuarial basis is not important – the important fact is that all LGPS funds are measured on the same assumptions, allowing comparison across funds.

3. DRY RUN

3.1 In preparation for the 2016 Section 13 valuation, GAD has carried out a reivew of the 2013 LGPS valuations against the criteria set out above. GAD has published its report and this is available on the link below.

http://www.lgpsboard.org/images/Reports/Section13DryRun20160711.pdf

3.2 The 2013 valuations pre-date the effective date of the legislation. As such, the work on the 2013 valuations has no legal force but serves as a 'dry run' to familiarise all parties with the process and sets expectations as to how the 2016 valuation review might be implemented.

4. DRY RUN RESULTS – LGPS

4.1 As anticipated, no compliance issues were found.

4.2 GAD reported that they had found both presentational and evidential inconsistencies in the valuation approach adopted by some LGPS funds, and in assumptions used and disclosure of results. These inconsistencies make meaningful comparison of local valuation results difficult.

4.3 GAD reported concerns over securing solvency for two passenger transport funds that are closed to new members. A number of funds raised amber flags on one or more metrics examined under solvency. No funds were red flagged.

4.4 GAD named two funds (Berkshire and Somerset) with whom they would have wanted to have further discussion over the long term cost efficiency of their funding plans (i.e. their employers may not be paying enough contributions to fully repay the deficits in the funds)

4.5 GAD clarified that meeting solvency and long term cost-efficiency requirements takes precedence in the regulatory framework over the desirability of stable contributions (which is an objective in the LGPS regulations).

5. DRY RUN RESULTS – GMPF

5.1 Using the standard set of assumptions, GMPF has a funding level of 103% at 31 March 2016. This is the joint 4th highest funding level across England and Wales. GMPF's funding level assessed using the Fund's own assumptions was 91%, this was the joint 5th highest.

5.2 There were no red flags for GMPF under either the solvency or long-term cost efficiency criteria. GMPF was one of several funds to receive an amber flag on one of the solvency sub-criteria. This sub-criteria is a measure of the amount that contributions would need to increase by should the value of return-seeking assets decrease by 15%. This largely reflects the maturity of GMPF's membership compared to the average LGPS fund. If a fund received amber flags on several sub-criteria then GAD may seek further discussion with the fund to determine whether any further action may be required.

6. COMMENT

6.1 The GAD Section 13 report should help ensure fair comparisons can be made between LGPS funds and reduce the number of funds showing artificially inflated funding levels based on highly optimistic assumptions about the future. This additional level of scrutiny will hopefully improve funding standards, increase transparency and enhance the understanding of stakeholders and commentators.

6.2 However, each LGPS fund is responsible for meeting its own liabilities and should be able to, in conjunction with its advisors, implement a funding approach that reflects its local situation, beliefs and attitude to risk. Considerable risks are introduced by taking an approach which encourages funds to set their funding plan by reference to either a standard basis or the approach adopted by other LGPS funds. These risks include less engagement and ownership of funding decisions, loss of diversification within the LGPS leading to a concentration of funding risk, loss of innovation and creative solutions to funding challenges and the adoption of unsuitable assumptions. Perhaps the most potentially damaging risk is heading towards a "minimum funding requirement" – often described as a "race to the bottom".

6.3 GAD has examined a number of metrics, all at whole of fund level. However, administering authorities and fund actuaries address funding challenges at the individual employer level and try to optimise both solvency and long term cost efficiency for every employer in the fund through the valuation process. There are considerable complexities in this process which will not be captured by examination of high-level whole fund results.

6.4 The primary purpose of the triennial funding valuations is to allow each administering authority to put in place a funding plan that levies adequate contributions from employers and invests assets appropriately in order to meet the liabilities of their individual LGPS fund. Section 13 can play a valuable role in reassuring stakeholders that the LGPS as whole is in a position to meet the benefits earned by members and to flag where individual funds appear to be outliers from the main pack. However, it would be counter-productive if, by having undue regard to how they appear under Section 13, funds compromised their funding valuations and reduced their chances of meeting their liabilities cost effectively - the tail should not wag the dog!

7. RECOMMENDATIONS

7.1 Members are recommended to note the report.