

APPENDIX 2  
London Borough of Haringey Pension Fund  
Funding Strategy Statement

## 1. Introduction

This is the Funding Strategy Statement (FSS) of the London Borough of Haringey Pension Fund, ("the Fund") that is administered by Haringey Council, ("the Administering Authority").

It has been prepared by the Administering Authority in collaboration with the Fund's actuary, Hymans Robertson LLP, and after consultation with the Fund's employers and investment adviser. This revised version replaces the previous Funding Strategy Statement and is effective from 31 March 2011.

### 1.1 Regulatory Framework

Scheme members' accrued benefits are guaranteed by statute. Members' contributions are fixed in the Regulations at a level that covers only part of the cost of accruing benefits. Employers currently pay the balance of the cost of delivering the benefits to members. The FSS focuses on the pace at which these liabilities are funded and, insofar as is practical, the measures to ensure that employers pay for their own liabilities.

The FSS forms part of a framework that includes:

- the Local Government Pension Scheme Administration Regulations 2008 (regulations 35, 36 and 38 are particularly relevant);
- the Rates and Adjustments Certificate, which can be found appended to this statement in Annex A and the Fund actuary's triennial valuation report;
- actuarial factors for valuing early retirement costs and the cost of buying extra service; and
- the Statement of Investment Principles.

This is the framework within which the Fund's actuary carries out triennial valuations to set employers' contributions, provides recommendations to the Administering Authority when other funding decisions are required, for example when employers join or leave the Fund. The FSS applies to all employers participating in the Fund.

The key requirements relating to the FSS are that:

- After consultation with all relevant interested parties involved with the Fund, the administering authority will prepare and publish their funding strategy.
- In preparing the FSS the administering authority must have regard to :
  - FSS guidance produced by CIPFA

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- It's Statement of Investment Principles published under Regulation 12 of the Local Government Pension Scheme (Management & Investment of Funds) Regulations 2009
- The FSS must be revised and published whenever there is a material change in either the policy on the matters set out in the FSS or the Statement of Investment Principles.

The Fund's actuary must have regard to the FSS as part of the fund valuation process.

## 1.2 Reviews of FSS

The FSS is reviewed in detail at least every three years in conjunction with triennial valuations being carried out, with the next full review due to be completed by 31 March 2014. More frequently, Annex A is updated to reflect any changes to employers.

The FSS is a summary of the Fund's approach to funding liabilities. It is not an exhaustive statement of policy on all issues. If you have any queries please contact Nicola Webb in the first instance at [Nicola.webb@haringey.gov.uk](mailto:Nicola.webb@haringey.gov.uk) or on 020-8489-3726.

## 2. **Purpose**

### 2.1 Purpose of FSS

The Department for Communities and Local Government (CLG) has stated that the purpose of the FSS is:

- *"to establish a clear and transparent fund-specific strategy which will identify how employers' pension liabilities are best met going forward;*
- *to support the regulatory framework to maintain as nearly constant employer contribution rates as possible; and*
- *to take a prudent longer-term view of funding those liabilities."*

These objectives are desirable individually, but may be mutually conflicting. Whilst the position of individual employers must be reflected in the statement, it must remain a single strategy for the Administering Authority to implement and maintain.

This statement sets out how the Administering Authority has balanced the conflicting aims of affordability of contributions, transparency of processes, stability of employers' contributions, and prudence in the funding basis across a range of employers participating in the Fund.

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## 2.2 Purpose of the Fund

The Fund is a vehicle by which scheme benefits are delivered. The Fund:

- receives contributions, transfer payments and investment income;
- pays scheme benefits, transfer values and administration costs.

One of the objectives of a funded scheme is to reduce the variability of pension costs over time for employers compared with an unfunded (pay-as-you-go) alternative.

The roles and responsibilities of the key parties involved in the management of the pension scheme are summarised in Annex B.

## 2.3 Aims of the Funding Policy

The objectives of the Fund's funding policy include the following:

- to ensure the long-term solvency of the Fund (and of the share of the Fund notionally allocated to individual employers);
- to ensure that sufficient funds are available to meet all benefits as they fall due for payment;
- not to restrain unnecessarily the investment strategy of the Fund so that the Administering Authority can seek to maximise investment returns (and hence minimise the cost of the benefits) for an appropriate level of risk;
- to help employers recognise and manage pension liabilities as they accrue;
- to minimise the degree of short-term change in the level of each employer's contributions where the Administering Authority considers it reasonable to do so;
- to use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations;
- to address the different characteristics of the disparate employers or groups of employers to the extent that this is practical and cost-effective; and
- to maintain the affordability of the Fund to employers as far as is reasonable over the longer term.

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## 3. Solvency Issues and Target Funding Levels

### 3.1 Derivation of Employer Contributions

Employer contributions are normally made up of two elements:

- a) the estimated cost of future benefits being accrued, referred to as the “*future service rate*”; plus
- b) an adjustment for the funding position (or “solvency”) of accrued benefits relative to the Fund’s solvency target, “*past service adjustment*”. If there is a surplus there may be a contribution reduction; if a deficit a contribution addition, with the surplus or deficit spread over an appropriate period.

The Fund’s actuary is required by the regulations to report the *Common Contribution Rate* (see regulation 36(4) of the Local Government Pension Scheme (Administration) Regulations 2008), for all employers collectively at each triennial valuation. It combines items (a) and (b) and is expressed as a percentage of pay. For the purpose of calculating the Common Contribution Rate, the surplus or deficit under (b) is currently spread over a period of 20 years.

The Fund’s actuary is also required to adjust the Common Contribution Rate for circumstances which are deemed “peculiar” to an individual employer (see regulation 36(7) of the Local Government Pension Scheme (Administration) Regulations 2008). It is the adjusted contribution rate which employers are actually required to pay. The sorts of “peculiar” factors which are considered are discussed in Section 3.5.

In effect, the *Common Contribution Rate* is a notional quantity. Separate future service rates are calculated for each employer together with individual past service adjustments according to employer-specific spreading and phasing periods. For some employers it may be agreed to pool contributions, see Section 3.7.8.

Annex A contains a breakdown of each employer’s contributions following the 2010 valuation for the financial years 2011/12, 2012/13 and 2013/14. It also identifies if employers’ contributions have been pooled with others.

Any costs of early retirements other than on the grounds of ill-health must be paid as lump sum payments at the time of the employer’s decision in addition to the contributions described above (or by instalments shortly after the decision).

Employers’ contributions are expressed as minima, with employers able to pay regular contributions at a higher rate. Employers should agree with the Administering Authority before making one-off capital payments.

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## 3.2 Solvency and Target Funding Levels

The Fund's actuary is required to report on the "solvency" of the whole fund at least every three years.

'Solvency' for ongoing employers is defined to be the ratio of the market value of assets to the value placed on accrued benefits on the Fund actuary's *ongoing funding basis*. This quantity is known as a funding level.

The ongoing funding basis is that used for each triennial valuation for all employers in the Fund. The on-going funding basis assumes employers in the Fund are an on-going concern and is described in the next section. The Fund actuary agrees the financial and demographic assumptions to be used for each such valuation with the Administering Authority.

The Fund operates the same target funding level for all ongoing employers of 100% of its accrued liabilities valued on the ongoing basis. The time horizon of the funding target may vary by employer depending on the expected duration of their participation in the Fund. Please refer to paragraph 3.8 for the treatment of departing employers.

## 3.3 Ongoing Funding Basis

The demographic assumptions are intended to be best estimates of future experience in the Fund based on past experiences of LGPS funds advised by the Fund Actuary. It is acknowledged that future life expectancy and in particular, the allowance for future improvements in mortality, is uncertain. Allowance has been made in the ongoing valuation basis for future improvements in line with "medium cohort" and a 1% minimum underpin to future reductions in mortality rates.

The approach taken is considered reasonable in light of the long term nature of the Fund and the assumed statutory guarantee underpinning members' benefits. The demographic assumptions vary by type of member and so reflect the different profiles of employers.

The key financial assumption is the anticipated return on the Fund's investments. The investment return assumption makes allowance for anticipated returns from the Fund's assets in excess of gilts. There is, however, no guarantee that assets will out-perform gilts. The risk is greater when measured over short periods such as the three years between formal actuarial valuations, when the actual returns and assumed returns can deviate sharply.

In light of the statutory requirement for the Actuary to consider the stability of employer contributions, it is therefore normally appropriate to restrict the degree of change to employers' contributions at triennial valuation dates.

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Given the very long-term nature of the liabilities, a long term view of prospective returns from equities is taken. For the 2010 valuation, it is assumed that the Fund's investments will deliver an average real additional return of 1.6% a year in excess of the return available from investing in index-linked government bonds at the time of the valuation. The long term in this context would be 20 to 30 years or more. In the opinion of the Fund Actuary, based on the current investment strategy of the Fund, an asset out-performance assumption (AOA) of 1.6% p.a. is within a range that would be considered acceptable for the purposes of the funding valuation.

Pay for public sector employees will be frozen by Government until 2012, with a flat increase of £250 being applied to all those earning less than £21,000 p.a. Although this "pay freeze" does not officially apply to local government employers, it has been suggested that they are expected to show similar restraint in respect of pay awards. Based on an analysis of the membership in LGPS funds, the average expected increase in pensionable pay across all employees should be around 1% p.a. for the next two years. Therefore the salary increase assumption at the 2010 valuation has been set to 1% p.a. for 2010/11 and 2011/12 for all employers. After this point, the assumption will revert back to RPI plus 1.5% p.a, as adopted for the previous valuation, although this will be subject to monitoring by the actuary to the Fund.

The Chancellor of the Exchequer announced in his Emergency Budget on 22 June 2010 that the consumer prices index (CPI) rather than the retail prices index (RPI) will be the basis for future increases to public sector pensions in payment and in deferment. This proposed change has been allowed for in the valuation calculations as at 31 March 2010.

At the 2007 valuation, the assumption for RPI was derived from market data as the difference between the yield on long-dated fixed interest and index-linked government bonds. At this valuation, we propose to adjust this market-derived rate downwards by 0.5% p.a. to allow for the "formula effect" of the difference between RPI and CPI. Basing pension increases on CPI rather than RPI will serve to reduce the value placed on the Fund's liabilities.

The demographic assumptions vary by type of member and so reflect the different membership profiles of employers. The same financial assumptions are adopted for all ongoing employers. All employers have the same asset allocation.

### 3.4 Future Service Contribution Rates

The future service element of the employer contribution rate is calculated on the ongoing valuation basis, with the aim of ensuring that there are sufficient assets built up to meet future benefit payments in respect of future service. The future service rate has been calculated

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separately for all the employers, although employers within a pool will pay the contribution rate applicable as a whole.

The approach used to calculate the employer's future service contribution rate depends on whether or not new entrants are being admitted.

Employers should note that it is only Admission Bodies that may have the power not to admit automatically all eligible new staff to the Fund, depending on the terms of their Admission Agreements and employment contracts.

### 3.4.1 *Employers that admit new entrants*

The employer's future service rate will be based upon the cost (in excess of members' contributions) of the benefits which employee members earn from their service each year. Technically these rates will be derived using the *Projected Unit Method* with a one year control period. This method calculates the contribution rate which meets the cost of benefits accruing in the year after the valuation date.

If future experience is in line with assumptions, and the employer's membership profile remains stable, this rate should be broadly stable over time. If the membership of employees matures (e.g. because of lower recruitment) the rate would rise.

### 3.4.2 *Employers that do not admit new entrants*

Certain Admission Bodies have closed the scheme to new entrants. This is expected to lead to the average age of employee members increasing over time and hence, all other things being equal, the future service rate is expected to increase as the membership ages.

To give more long term stability to such employers' contributions, the *Attained Age* funding method is normally adopted. This method anticipates the ageing of the membership and, for a closed employer, would lead to a stable total contribution rate if the assumptions are borne out in practice. This will limit the degree of future contribution rises by paying higher rates at the outset.

Both funding methods are described in the Actuary's report on the valuation.

Both future service rates will include an allowance for expenses of administration to the extent that they are borne by the Fund and include an allowance for benefits payable on death in service and ill health retirement.

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### 3.5 Adjustments for Individual Employers

Adjustments to individual employer contribution rates are applied both through the calculation of employer-specific future service contribution rates and the calculation of the employer's funding position.

The combined effect of these adjustments for individual employers applied by the Fund actuary relate to:

- past contributions relative to the cost of accruals of benefits;
- different liability profiles of employers (e.g. mix of members by age, gender, part-time/full-time, manual/non manual);
- the effect of any changes to the valuation basis from the one used in the previous valuation, on the value placed on the employer's liabilities;
- any different deficit/surplus spreading periods or phasing of contribution changes;
- the difference between actual and assumed rises in pensionable pay;
- the difference between actual and assumed increases to pensions in payment and deferred pensions;
- the difference between actual and assumed retirements on grounds of ill-health from active status;
- the difference between actual and assumed amounts of pension ceasing on death;
- the additional costs of any non ill-health retirements relative to any extra payments made;

over the period between the 2007 and 2010 valuations and each subsequent triennial valuation period.

Actual investment returns achieved on the Fund between each valuation are applied proportionately across all employers. Transfers of liabilities between employers within the Fund occur automatically within this process, with a sum broadly equivalent to the reserve required on the ongoing basis being exchanged between the two employers.

The Fund actuary does not allow for certain relatively minor events occurring in the period since the last formal valuation, including, but not limited to:

- the actual timing of employer contributions within any financial year; and
- the effect of the premature payment of any deferred pensions on grounds of incapacity.



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These effects are swept up within a miscellaneous item in the analysis of surplus, which is split between employers in proportion to their liabilities.

### 3.6 Asset Share Calculations for Individual Employers

The Administering Authority does not account for each employer's assets separately. The Fund's actuary is required to apportion the assets of the whole Fund between the employers (or pool of employers) at each triennial valuation using the income and expenditure figures provided for certain cash flows for each employer or pool of employers. This process adjusts for transfers of liabilities between employers participating in the Fund, but does make a number of simplifying assumptions. The split is calculated using an actuarial technique known as "analysis of surplus". The methodology adopted means that there will inevitably be some difference between the asset shares calculated for individual employers and those that would have resulted had they participated in their own ring-fenced section of the Fund. The asset apportionment is capable of verification but not to audit standard.

The Administering Authority recognises the limitations in the process, but having regard to the extra administration cost of building in new protections, it considers that the Fund actuary's approach addresses the risks of employer cross-subsidisation to an acceptable degree.

### 3.7 Stability of Employer Contributions

#### 3.7.1 *Solvency issues and target funding levels*

In setting employer contribution rates, the Administering Authority must balance the aims of stability and affordability with the requirement to take a prudent, longer-term view of funding and ensure the solvency of the Fund. The more secure the employer, the more emphasis can be placed on stability of employer contributions without jeopardising the Administering Authority's commitment to prudent stewardship of the Fund. For the most secure, long term employers an explicit stabilisation overlay based on a risk-based, stochastic valuation approach is used (see para 3.7.2).

For less secure and shorter term employers (principally, but not exclusively, the admission bodies) it is generally not possible to achieve the same degree of stability in employer contribution rates without compromising on prudent stewardship. However, other measures such as re-lengthening deficits recovery periods, phasing in of employer contribution increases or pooling help achieve a greater degree of stability of employer contributions than would otherwise be the case. Further, in cases where employers provide additional security to the Fund, the Administering Authority may, at its discretion, be prepared to agree to employer contributions below the theoretical rate derived from the valuation results.

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The Administering Authority's policies in respect of the use of these approaches are set out in the remainder of 3.7 and in 3.8 below.

### 3.7.2 *Stabilisation*

For the most secure, long term employers there is an explicit stabilisation overlay. The stabilisation mechanism analyses a number of metrics over the long-term including the evolution of the funding level to check the likelihood of achieving the solvency of the Fund over the longer-term under a variety of contribution strategies. This analysis enables the Administering Authority to reduce the effect of short term investment market volatility on the contribution rates of eligible employers.

#### *Stabilisation overlay rules and eligibility*

Under the stabilisation overlay, variations in the employer contribution rate from year to year are kept within a pre-determined range so that eligible employers' contribution rates can remain relatively stable. Only precepting employers are eligible for stabilisation.

The stabilisation overlay rules for eligible employers are

- No increases for the period 1 April 2011 to 31 March 2014; and
- Maximum change of 1% p.a. thereafter.

#### Notes:

- 1) Increases and reductions apply over the three year period between valuations;
- 2) Increases and reductions are relative to rates certified at the previous valuation.

#### *Circumstances in which eligibility for stabilisation will be reviewed*

- The Administering Authority may review an employer's eligibility for stabilisation at any time in the event of significant changes in the employer's membership (due for example to redundancies or outsourcing) or if there is a significant change in the Administering Authority's assessment of an employer's security.
- Stabilisation rules and eligibility may be reviewed at any time in the event of changes to scheme benefits. Changes in scheme benefits may arise because of changes in regulations or other events that have a material impact (such as the change with effect from April 2011 from RPI to CPI for increases to pensions in payment).
- The stabilisation rules and eligibility criteria will be reviewed no later than at the 31 March 2013 valuation, with any changes in contribution strategy taking effect from 1 April 2014. The review will take into account factors including, but not necessarily restricted to, market conditions (the long-term risk-based analysis will be recalibrated to market conditions as at 31 March 2013), the

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Administering Authority's assessment of employer's security and the maturity of each employer's membership profile.

### *Setting the parameters of the stabilisation overlay*

The parameters for the stabilisation overlay have been determined by carrying out an asset liability modelling exercise. This allows for the future uncertainty in investment returns, interest rates and inflation using a stochastic modelling technique. The actuary tested the contribution stabilisation rules to ensure that they were compatible with the current investment strategy. He has advised the Administering Authority that the stabilisation overlay for secure long term secure employers satisfies the requirement for the funding strategy to take a prudent longer-term view based on a reasonably prudent ongoing funding basis.

### 3.7.3 *Deficit Recovery Periods*

The Administering Authority normally targets the recovery of any deficit over a period not exceeding 20 years. However, these are subject to the maximum lengths set out in the table below unless otherwise agreed by the Administering Authority and the Fund's actuary.

| <b>Type of Employer</b>                            | <b>Maximum Length of Deficit Recovery Period</b>   |
|--|--|
| Statutory bodies with tax raising powers           | A period to be agreed with each employer not exceeding 20 years.   |
| Scheduled Bodies                                   | A period to be agreed with each employer depending on the strength of their covenant, but not exceeding 20 years.  |
| Community Admission Bodies with funding guarantees | A period to be agreed with each employer depending on the terms of the guarantee, but not exceeding 20 years.  |
| Transferee Admission Bodies                        | The period from the start of the revised contributions to the end of the employer's contract.  |
| All other types of employer                        | A period to be agreed with each employer depending on the strength of their covenant; this will generally be equivalent to the expected future working lifetime of the remaining scheme members. |

This *maximum* period (unless otherwise agreed by the Administering Authority and the Fund's actuary) is used in calculating each employer's *minimum* contributions. Employers may opt to pay higher regular contributions than these minimum rates.

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The deficit recovery period starts at the commencement of the revised contribution rate (1 April 2011 for 2010 valuation).

### *3.7.4 Deficit Recovery Payments*

For employers where stabilisation is not being applied, the deficit recovery payments for each employer covering the three year period until the next valuation will usually be set as a percentage of salaries. However, the Administering Authority reserves the right to amend these rates between valuations and/or to require these payments in monetary terms instead, for instance where:

- the employer is an admitted body with a relatively large deficit recovery contribution rate, or
- there has been a significant reduction in payroll due to outsourcing or redundancy exercises, or
- the employer has closed the Fund to new entrants.

### *3.7.5 Surplus Spreading Periods*

For any employer deemed to be in surplus, the approach is to maintain contributions at no less than the assessed future service level. At the Administering Authority's discretion however, employers may be permitted to reduce their contributions below the cost of accruing benefits, by spreading the surplus element over the maximum periods shown above for deficits in calculating their minimum contributions.

However if they take the full benefit of their surplus re-payments then their ability to withstand future adverse shocks in the 2013 valuation will be diminished. Employers should consider carefully whether or not to take the full benefit of their current surplus.

### *3.7.6 Phasing in of Contribution Rises*

Transferee Admission Bodies are not eligible for phasing in of contribution rises. Other employers may opt to phase in contribution rises over a three year period providing they pay a minimum of the future service rate.

### *3.7.7 Phasing in of Contribution Reductions*

Any contribution reductions will be phased in over three years for all employers except Transferee Admission Bodies who can take the reduction with immediate effect.

### *3.7.8 The Effect of Opting for Longer Spreading or Phasing-In*

Employers which are permitted and elect to use a longer deficit spreading period than was used at the 2007 valuation, or to phase-in contribution changes, will be assumed to incur a greater loss of

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investment returns on the deficit by opting to defer repayment. Therefore, deferring paying contributions will lead to higher contributions in the long-term (depending on the actual financial and demographic performance of the Fund relative to the valuation assumptions).

However any adjustment is expressed for different employers, the overriding principle is that the discounted value of the contribution adjustment adopted for each employer will be equivalent to the employer's deficit.

### 3.7.9 *Pooled Contributions*

The Administering Authority currently allows Haringey Council to pool the legacy liabilities and assets that remain when an employer leaves the Fund. The Administering Authority will consider the arguments for pooling on a case by case basis, but in general does not permit the pooling of contribution rates.

### 3.7.10 *Regular Reviews*

The Administering Authority reserves the right to review contribution rates and amounts and the level of security provided, at regular intervals. These intervals may be annual, in the case of Admission Bodies and/or in the last few years of the employer's contract. Such reviews may be triggered by significant reductions in payroll, altered employer circumstances, Government restructuring affecting the employer's business or failure to pay contributions or arrange appropriate security as required by the Administering Authority.

The result of a review may be to require increased contributions payable (by strengthening the actuarial assumptions adopted and/or moving to monetary levels of deficit recovery contributions), an increased level of security or guarantee, or some combination of these.

### 3.8 Admission Bodies ceasing

Admission Agreements for Best Value contractors are assumed to expire at the end of the contract.

Admission Agreements for other employers are generally assumed to be open-ended and to continue until the last pensioner dies. Contributions, expressed as capital payments, can continue to be levied after all the employees have retired. These Admission Agreements can however be terminated at any point.

The Fund, however, considers any of the following as triggers for the termination of an admission agreement:

- Last active member ceasing participation in the LGPS;

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- The insolvency, winding up or liquidation of the admission body;
- Any breach by the Admission Body of any of its obligations under the agreement that they have failed to remedy to the satisfaction of the Fund;
- A failure by the admission body to pay any sums due to the Fund within the period required by the Fund; or
- The failure by the admission body to renew or adjust the level of the bond or indemnity or to confirm appropriate alternative guarantor as required by the Fund.

In addition either party can voluntarily terminate the admission agreement by giving the appropriate period of notice as set out in the admission agreement to the other party (or parties in the case of a Transferee Admission Body).

If an Admission Body's admission agreement is terminated, the Administering Authority instructs the Fund actuary to carry out a special valuation to determine whether there is any deficit.

The assumptions adopted to value the departing employer's liabilities for this valuation will depend upon the circumstances. For example:

- (a) For Transferee Admission Bodies, the assumptions would be those used for an ongoing valuation to be consistent with those used to calculate the initial transfer of assets to accompany the active member liabilities transferred.
- (b) For non-Transferee Admission Bodies that elect to voluntarily terminate their participation, the Administering Authority must look to protect the interests of other ongoing employers and will require the actuary to adopt valuation assumptions which, to the extent reasonably practicable, protect the other employers from the likelihood of any material loss emerging in future. In order to protect other employers in the Fund, the cessation liabilities and final deficit will normally be calculated using a "gilts cessation basis" with no allowance for potential future investment outperformance and with an allowance for further future improvements in life expectancy. This approach results in a higher value being placed on the liabilities than would be the case under a valuation on the ongoing funding basis and could give rise to significant payments being required.
- (c) For Admission Bodies with guarantors or a successor body, it is possible that any deficit could be transferred to the guarantor/successor in which case it may be possible to simply transfer the former Admission Bodies members and assets to the guarantor/successor, without needing to crystallise any deficit.

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Under (a) and (b), any shortfall would be levied on the departing Admission Body as a capital payment.

As an alternative to (b) above where the ceasing Admission Body is continuing in business, the Fund, at its absolute discretion, reserves the right to enter into an agreement with the ceasing Admission Body to accept an appropriate alternative security to be held against any funding deficit and to carry out the cessation valuation on an ongoing valuation basis. This approach would be monitored as part of each triennial valuation and the Fund reserves the right to revert to a "gilts cessation basis" and seek immediate payment of any funding shortfall identified.

In the event that the Fund is not able to recover the required payment in full directly from the Admission Body or from any bond or indemnity or guarantor, then:

- a. In the case of Transferee Admission Bodies the awarding authority will be liable. At its absolute discretion, the Administering Authority may agree to recover any outstanding amounts via an increase in the awarding authority's contribution rate over an agreed period.
- b. In the case of admission bodies that are not Transferee Admission Bodies and have no guarantor, the unpaid amounts fall to be shared amongst all of the employers in the Fund. This will normally be reflected in contribution rates set at the formal valuation following the cessation date.

### 3.9 Early Retirement Costs

#### 3.9.1 *Non Ill Health retirements*

The actuary's funding basis makes no allowance for premature retirement except on the grounds of ill-health. All employers are required to pay additional contributions wherever an employee retires "early" (see below) with no reduction to their benefit or receives an enhanced pension on retirement.

It is assumed that members' benefits on age retirement are payable from the earliest age that the employee could retire without incurring a reduction to their benefit and without requiring their employer's consent to retire. Members receiving their pension unreduced before this age other than on ill-health grounds are deemed to have retired "early".

The additional costs of premature retirement are calculated by reference to these ages. Employers must make these additional contributions as a one off payment to the Fund immediately on awarding the early retirement.

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### 3.9.2 *Ill health monitoring*

The Fund monitors each employer's ill health experience on an ongoing basis. If the cumulative number of ill health retirements in any financial year exceeds the allowance at the previous valuation, the employer will be charged additional contributions on the same basis as applies for non ill-health cases.

### 3.9.3 *Ill health insurance*

Employers have the ability to insure ill health early retirement strains through a policy that can currently be arranged with Legal & General. Where this insurance is effected:

- the employer's contribution to the Fund each year is reduced by the amount of that year's insurance premium, so that the total contribution is unchanged;
- there is no need for monitoring of allowances.

### 3.10 New admitted bodies

The Fund requires the following from any potential Admission Bodies wishing to join the Fund.

Transferee Admission Bodies will be required to have a guarantee from the transferring scheduled body and also provide a bond if requested by the Administering Authority. The bond is required to cover the following:

- the strain cost of any redundancy early retirements resulting from the premature termination of the employer's contract
- allowance for the risk of asset underperformance
- allowance for the risk of a fall in gilt yields
- allowance for unpaid contributions

The employer may also be required to include their current deficit within the bond amount. The bond will be reassessed on an annual basis.

When the Administering Authority considers requests from Community Admission Bodies to join the Fund, they will be seeking sponsorship for the Body from a scheduled body with tax raising powers guaranteeing their liabilities and also if appropriate a bond.

This reduces the risk to the Fund of potentially having to pick up any shortfall in respect of Admission Bodies.



#### 4. Links to Investment Strategy

Funding and investment strategy are inextricably linked. Investment strategy is set by the administering authority, after consultation with the employers and after taking investment advice.

##### 4.1 Investment Strategy

The investment strategy currently being pursued is described in the Fund's Statement of Investment Principles.

The investment strategy is set for the long-term, but is reviewed from time to time, normally every three years, to ensure that it remains appropriate to the Fund's liability profile. The Administering Authority has adopted a benchmark, which sets the proportion of assets to be invested in key asset classes such as equities, bonds and property. As at 31 March 2010, the proportion held in equities and property was 72% of the total Fund assets.

The investment strategy of lowest risk would be one which provides cash-flows which replicate the expected benefit cash-flows (i.e. the liabilities). Equity investment would not be consistent with this.

The Fund's benchmark includes a significant holding in equities in the pursuit of long-term higher returns than from a liability matching strategy. The Administering Authority's strategy recognises the relatively immature liabilities of the Fund and the secure nature of most employers' covenants.

The same investment strategy is currently followed for all employers. The Administering Authority does not currently have the facility to operate different investment strategies for different employers.

##### 4.2 Consistency with Funding Basis

The key financial assumption is the anticipated return on the Fund's investments. The investment return assumption makes allowance for anticipated returns from equities in excess of bonds. There is, however, no guarantee that equities will out-perform bonds. The risk is greater when measured over short periods such as the three years between formal actuarial valuations, when the actual returns and assumed returns can deviate sharply. It is therefore normally appropriate to restrict the degree of change to employers' contributions at triennial valuation dates.

In the opinion of the Fund actuary, the current funding policy is consistent with the current investment strategy of the Fund, the asset outperformance assumption is within a range that would be considered acceptable for the purposes of the funding valuation and consistent with the requirement to take a "prudent longer-term view" of the funding

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of liabilities (see para 2.1). The same financial assumptions are adopted for all employers which fund on the ongoing basis. However, low risk financial assumptions are adopted for all employers which fund on the low risk basis.

However, in the short term – such as the three yearly assessments at formal valuations – there is the scope for considerable volatility and asset returns may fall short of this target. The stability measures described in Section 5 will damp down, but not remove, the effect on employers' contributions.

The Fund does not hold a contingency reserve to protect it against the volatility of equity investments.

### 4.3 Balance between risk and reward

Prior to implementing its current investment strategy, the Administering Authority considered the balance between risk and reward by altering the level of investment in potentially higher yielding, but more volatile, asset classes like equities.

### 4.4 Inter-valuation monitoring of funding position

The Administering Authority monitors investment performance relative to the growth in the liabilities by means of annual interim valuations. If appropriate, investigations will also be made into the individual employer funding positions.

## 5. **Key Risks & Controls**

### 5.1 Types of Risk

The Administering Authority has an active risk management programme in place. The measures that the Administering Authority has in place to control key risks are summarised below under the following headings:

- Financial;
- Demographic;
- Regulatory; and
- Governance.

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5.2 Financial Risks

| <b>Risk</b>   | <b>Summary of Control Mechanisms</b>  |
|---|---|
| Fund assets fail to deliver returns in line with the anticipated returns underpinning valuation of liabilities over the long-term | <p><i>Only anticipate long-term return on a relatively prudent basis to reduce risk of under-performing.</i></p> <p><i>Analyse progress at three yearly valuations for all employers.</i></p> <p><i>Annual interim valuations.</i></p>  |
| Inappropriate long-term investment strategy   | <i>Set a Fund-specific benchmark following receipt of professional investment advice.</i>   |
| Fall in risk-free returns on Government bonds, leading to rise in value placed on liabilities                                     | <p><i>Inter-valuation monitoring, as above.</i></p> <p><i>Some investment in bonds helps to mitigate this risk.</i></p>   |
| Active investment manager under-performance relative to benchmark   | <i>Short term (quarterly) investment monitoring analyses market performance and active managers relative to their index benchmark and target.</i>   |
| Pay and price inflation significantly more than anticipated   | <p><i>The focus of the actuarial valuation process is on real returns on assets, net of price and pay increases.</i></p> <p><i>Inter-valuation monitoring, as above, gives early warning.</i></p> <p><i>Some investment in index linked bonds also helps to mitigate this risk.</i></p> <p><i>Employers pay for their own salary awards and are reminded of the geared effect on pension liabilities of any bias in pensionable pay rises towards longer-serving employees.</i></p> |
| Effect of possible increase in employer's contribution rate on service delivery and admission/scheduled bodies                    | <p><i>Seek feedback from employers on scope to absorb short-term contribution rises.</i></p> <p><i>Mitigate impact through deficit spreading and phasing in of contribution rises.</i></p>  |

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5.3 Demographic Risks

| <b>Risk</b>  | <b>Summary of Control Mechanisms</b>   |
|--|--|
| Ill-health retirements significantly more than anticipated.  | <i>Monitoring of each employer's ill-health experience on an ongoing basis. The employer may be charged additional contributions if this exceeds the ill-health assumptions built in.</i>  |
| Pensioners living longer.  | <i>Set mortality assumptions with some allowance for future increases in life expectancy.<br/><br/>Fund actuary monitors combined experience of around 50 funds to look for early warnings of lower pension amounts ceasing than assumed in funding.</i> |
| Deteriorating patterns of early retirements.   | <i>Employers are charged the extra capital cost of non ill health retirements following each individual decision.<br/><br/>Employer ill health retirement experience is monitored.</i>   |
| Maturing Fund i.e. proportion of actively contributing employees declines relative to retired employees. | <i>Continue to monitor at each valuation, consider seeking monetary amounts rather than percentage of pay and consider alternative investment strategies.</i>  |

5.4 Regulatory

| <b>Risk</b>   | <b>Summary of Control Mechanisms</b>   |
|---|--|
| Changes to regulations, e.g. more favourable benefits package, potential new entrants to scheme, e.g. part-time employees   | <i>The Administering Authority is alert to the potential creation of additional liabilities and administrative difficulties for employers and itself.</i>  |
| Changes to national pension requirements and/or HM Revenue and Customs rules e.g. effect of abolition of earnings cap for post 1989 entrants from April 2006, abolition of 85 year rule and new 2008 scheme | <i>The Administering Authority considers all consultation papers issued by the CLG and comments where appropriate.<br/><br/>The Administering Authority will consult employers where it considers that it is appropriate</i> |

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5.5 Governance

| Risk   | Summary of Control Mechanisms  |
|--|--|
| Administering Authority unaware of structural changes in an employer's membership (e.g. large fall in employee members, large number of retirements).                            | <i>The Actuary may be instructed to consider revising the rates and Adjustments certificate to increase an employer's contributions (under Regulation 38) between triennial valuations</i>   |
| Administering Authority not advised of an employer closing to new entrants.  | <i>Deficit contributions are expressed as monetary amounts and percentages (see Annex A).</i>  |
| Administering Authority failing to commission the Fund Actuary to carry out a termination valuation for a departing Admission Body and losing the opportunity to call in a debt. | <i>The Administering Authority requires employers with Best Value contractors to inform it of forthcoming changes.<br/><br/>It also operates a diary system to alert it to the forthcoming termination of Best Value Admission Agreements.</i>   |
| An employer ceasing to exist with insufficient funding or adequacy of a bond.  | <i>The Administering Authority believes that it would normally be too late to address the position if it was left to the time of departure.<br/><br/>The risk is mitigated by:</i> <ul style="list-style-type: none"> <li>• <i>Seeking a funding guarantee from another scheme employer, or external body, wherever possible.</i></li> <li>• <i>Alerting the prospective employer to its obligations and encouraging it to take independent actuarial advice.</i></li> <li>• <i>Vetting prospective employers before admission.</i></li> <li>• <i>Where permitted under the regulations requiring a bond to protect the scheme from the extra cost of early retirements on redundancy if the employer failed.</i></li> </ul> |

**Annex A – Employers’ Contributions, Spreading and Phasing Periods**

Following the 2010 valuation, the minimum employer contributions shown in the Rates and Adjustment certificate attached to the 2010 valuation report are based on the deficit recovery periods and phasing periods shown in the table below.

| Employer code | Employer name                                     | Contributions currently being paid in 2010/11 | Minimum Contributions for the Year Ending |                     |                     |
|---------------|---|---|---|---------------------|---------------------|
|               |   |   | 31 March 2012                             | 31 March 2013       | 31 March 2014       |
| 1             | Haringey Council                                  | 22.9%   | 22.9%                                     | 22.9%               | 22.9%               |
| 3             | Age Concern Haringey                              | 33.8%   | 22.6% plus £32,000                        | 22.6% plus £32,000  | 22.6% plus £34,000  |
| 5             | College of Enfield and North East London (CHENEL) | 19.9%   | 17.2% plus £303,000                       | 17.2% plus £468,000 | 17.2% plus £662,000 |
| 7             | Haringey Citizens Advice Bureaux                  | 19.6%   | 21.7% plus £22,000                        | 21.7% plus £22,000  | 21.7% plus £23,000  |
| 8             | Alexandra Palace Trading Co Ltd                   | 18.7%   | 23.0% plus £41,000                        | 23.0% plus £41,000  | 23.0% plus £43,000  |
| 11            | Urban Futures London Ltd                          | 17.4%   | 19.5% plus £28,000                        | 19.5% plus £29,000  | 19.5% plus £30,000  |
| 13            | Greig City Academy                                | 13.0%   | 16.8% plus £8,000                         | 16.8% plus £8,000   | 16.8% plus £8,000   |
| 18            | Homes for Haringey                                | 15.4%   | 18.3% plus £69,000                        | 18.3% plus £70,000  | 18.3% plus £74,000  |
| 19            | John Loughborough                                 | 17.2%   | 18.9%                                     | 18.9%               | 18.9%               |
| 20            | TLC at Coopercroft                                | 19.0%   | 25.4%                                     | 25.4%               | 25.4%               |
| 22            | Fortismere School                                 | 18.1%   | 19.2% plus £25,000                        | 19.2% plus £25,000  | 19.2% plus £27,000  |
| 23            | RM Education PLC                                  | 12.3%   | 17.6%                                     | 17.6%               | 17.6%               |
| 25            | Ontime Parking Solutions                          | 21.4%   | 22.1%                                     | 22.1%               | 22.1%               |
| 26            | ESSL  | 28.0%   | 24.6%                                     | 24.6%               | 24.6%               |

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**Annex B – Responsibilities of Key Parties**

*The Administering Authority should:*

- collect employer and employee contributions;
- invest surplus monies in accordance with the regulations;
- ensure that cash is available to meet liabilities as and when they fall due;
- manage the valuation process in consultation with the fund's actuary;
- prepare and maintain a Funding Strategy Statement and Statement of Investment Principles, both after proper consultation with interested parties;
- monitor all aspects of the fund's performance and funding and amend Funding Strategy Statement and Statement of Investment Principles as necessary;
- prepare annual accounts and get these audited, control cash flow and administration costs.

*The Individual Employer should:*

- deduct contributions from employees' pay correctly;
- pay all contributions, including their own as determined by the actuary, promptly by the due date;
- exercise discretions within the regulatory framework;
- make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of scheme benefits, early retirement strain, excess ill-health early retirements if appropriate;
- notify the administering authority promptly of all changes to membership or, as may be proposed, which affect future funding.

*The Fund actuary should:*

- prepare valuations including the setting of employers' contribution rates after agreeing assumptions with the Administering Authority and having regard to the Funding Strategy Statement;
- prepare advice and calculations in connection with bulk transfers and individual benefit-related matters.

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### The Pensions Committee should:

- carry out statutory functions relating to local government pensions under regulations made under Sections 7, 12 and 24 of the Superannuation Act 1972. Broadly this enables them to oversee the general framework within which the Fund is managed
- monitor investment and administration performance
- carry out regular reviews of investments and investment strategy
- determine and keep under constant review, an overall asset allocation policy for the Fund, including appointment and termination of fund managers
- consider appropriate professional advice on all matters with a material impact on the Scheme
- approve significant internal decisions and documents for the scheme including the valuation, Annual Report and Accounts and the FSS, and
- determine and keep under constant review, all policies and strategies of the Fund.