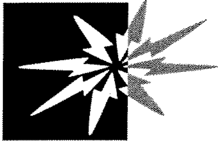


Pensions Committee **On 29 January 2008**

Report title: Triennial actuarial valuation and revised Funding Strategy Statement

Report of: Chief Financial Officer

Ward(s) affected: All	**Report for: Decision**

1. Purpose

1.1 To report the results of the triennial actuarial valuation as at 31 March 2007.

1.2 To report the revised Funding Strategy Statement (FSS) for approval.

2. Recommendations

2.1 That the results of the triennial actuarial valuation as at 31 March 2007 be noted.

2.2 That the revised Funding Strategy Statement be approved.

Report authorised by: Gerald Almeroth – Chief Financial Officer

Contact officer: John Hardy, Head of Finance-Budgeting, Projects & Treasury (tel no: 020 8489 3726)

3. Executive Summary

3.1 This report sets out the results of the triennial actuarial valuation as at 31 March 2007 for noting and our revised Funding Strategy Statement for approval.

3.2 The level of funding has increased from 69 per cent as at 31 March 2004 to 77.7 per cent as at 31 March 2007.

3.3 Following the 2007 valuation, the Actuary has agreed that the Council's contribution rate can prudently remain at the 2007/08 rate of 22.9 per cent.

3.4 The Actuary will issue the required report on the triennial valuation shortly and the required rates and adjustments certificate for each admitted, scheduled body and for the Council in March 2008.

3.5 It was deemed to be the right time to revise our Funding Strategy Statement (FSS). We received advice from our Actuary and have also shared the revised Statement with Admitted Bodies, Scheduled Bodies and the Independent Advisor to Trustees for any comments.

4. Reasons for any change in policy or for new policy development (if applicable)

No changes are proposed.

5. Local Government (Access to Information) Act 1985

The following background papers were used in the preparation of this report:

Report of Actuary as at 31 March 2007.

Current Funding Strategy Statement (FSS).

6. Background

6.1 The Fund is independently valued every three years by a firm of actuaries to assess the adequacy of the Fund's investments and contributions to meet its liabilities. This report considers the latest formal valuation that took place as at 31 March 2007.

7. Actuarial valuation

7.1 This actuarial review was carried out in accordance with Guidelines GN9: Retirement Benefits Schemes – Actuarial reports published by the Institute of Actuaries and the Faculty of Actuaries. Economic and statistical assumptions were used. The resulting contribution rates reflect the cost of providing year-by-year accrual of benefits for the Fund's members and the level of funding for each employer's past-service liabilities.

7.2 The funding level of the Pensions Fund at the 2004 valuation was 69 per cent and this has increased to 77.7 per cent as at the 2007 valuation (31 March 2007). The latter compares with an interim actuarial funding level of 79.8 per cent (based upon the 2004 valuation data) that was reported to Pensions Committee on 25 June 2007. The Haringey Council part of the fund has a funding level of 75 per cent as at 31 March 2007.

7.3 Following the 2007 valuation, the Actuary has agreed that the Council's contribution rate can prudently remain at the 2007/08 rate of 22.9 per cent.

7.4 The above contribution rate has been allowed for in the budget. The Financial Planning report is being considered by Cabinet on 22 January 2008.

7.5 The Actuary is present at this meeting to go through his main valuation findings as included in Appendix One.

7.6 The valuation takes into account implementation of the aspects of the 'new look' scheme due to come into effect from April 2008.

7.7 The increase in funding level from 69 per cent as at 31 March 2004 to 77.7 per cent as at 31 March 2007 is due to an improvement in investment earnings and value, and the planned stepped increases in employers contributions from 2004.

7.8 More specifically the change in funding level is largely explained on the good side by better than anticipated investment returns of 13.1% per annum (that is 6.3% per annum more than the discount rate). This adds around 14% to the funding level. Additional employer contributions made towards the past service deficit have contributed around 4% to the funding level improvement. This is offset by a fall in real gilt yields from 1.8% per annum to 1.3% per annum, changes in anticipated inflation, long term interest rates and demographic assumptions, reducing the funding level by 9%. An additional mortality reserve reduces the funding level by around 3%. Finally other items over the three year period adds around 3% to the funding level.

7.9 The Actuary has undertaken numerous validation checks of the data supplied to ensure that the calculations made are accurate. A good process was followed with data being provided to the Actuary on time and with not many errors.

7.10 In arriving at the results of the actuarial valuation, our funding strategy for 2007 is in line with that used for the 2004 valuation, namely;

- an assumption that the assets of the fund will outperform Government bonds by 1.6% per annum;
- the use of a 20 year deficit recovery period over which the past service deficit will be funded;
- the use of a 50% take up rate for commutation in line with government assumptions;
- some further increases in pensioner longevity.

7.11 The Actuary will issue the Fund's required report on the triennial valuation shortly. The rates and adjustments certificate for each admitted and scheduled body and for the Council will be issued in March 2008.

Key comparative data is as follows:

Valuation date	2004	2007
	£m	£m
Past service liabilities (whole fund)		
Employees	242.8	354.7
Deferred pensioners	101.8	153.6
Pensioners	242.9	289.9
Total liabilities	**587.4**	**798.2**
Assets	405.3	620.0
Surplus/(deficit)	**(182.1)**	**(178.1)**
Funding level	**69%**	**77.7%**
Contribution rates (Council only)		
Future service rate	12.8%	14.0%
Past service rate	10.1%	8.9%
Common contribution rate	**22.9%**	**22.9%**

7.12 A consultation meeting took place with admitted and scheduled bodies this afternoon (29 January 2008). In advance of this meeting detailed results were sent to each body by the Actuary. This meeting was chaired by the Chair of Pensions Committee. Any comments will be reported verbally at this meeting of the Committee.

8. Funding Strategy Statement

8.1 It was deemed to be the right time to revise our Funding Strategy Statement (FSS). We received advice from our Actuary and have also shared the revised Statement with Admitted Bodies, Scheduled Bodies and the Independent Advisor to Trustees for any comments.

8.2 The FSS has been updated by having regard to our own Statement of Investment Principles (SIP) and guidance published by CIPFA on preparing and maintaining a funding strategy statement. Our proposed revised FSS is shown in Appendix Two.

8.3 The main changes made are as follows:

- Page 4 of the FSS - an additional objective of the Fund's funding policy has been added, namely 'to maintain the affordability of the Fund to employers as far as is reasonable over the longer term.'

- Page 6 of the FSS - ongoing funding basis – we have expanded the FSS to include '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 for improvements in line with PMA/PFA92 series projections up to calendar year 2017 for non-pensioners and 2033 for pensioners with age ratings applied to fit past LGPS experience. Employers are aware that their contributions are likely to increase in future if longevity exceeds the funding assumptions.

  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.'

- Page 19 of the FSS – demographic risks – we have added an additional risk re the possibility of ill health retirements being significantly more than anticipated. Our control mechanism is '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.'

- Page 22 of the FSS (Annex A) – employers' contributions, spreading and phasing periods will be added once the Actuary supplies the certificate in March 2008.

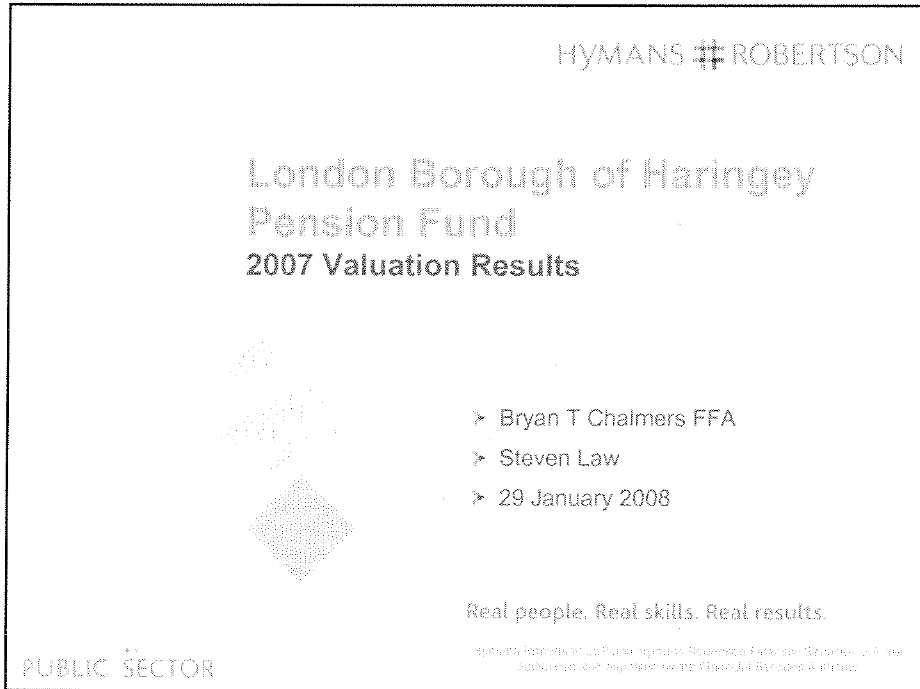
8.4 The revised FSS, if agreed, will become effective from 31 March 2008 to link in with receipt of the required certificate of contribution rates for each admitted and scheduled body and for the Council.

9. Comments of the Head of Legal Services

9.1 The Head of Legal Services has been consulted on the content of this report. Regulation 77 of the Local Government Pension Scheme Regulations 1997 (as amended) provides that an administering authority must obtain an actuarial valuation of the assets and liabilities of their pension fund at intervals of three years commencing 31 March 1998. The valuation must be accompanied by a report of the actuary and a rates and adjustments certificate.

9.2 Regulation 76A of the 1997 Regulations requires each administering authority to prepare, maintain and publish a written statement setting out their funding strategy. The first such statement is to have been published on or before 31 March 2005 and shall be revised and published by the authority following any material change in their policy on the matters set out in the statement. In preparing and maintaining the statement, the Authority must have regard to its own statement of investment principles and the guidance published by CIPFA on preparing and maintaining a funding strategy statement.

APPENDIX ONE

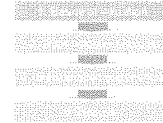


Agenda

1. Basics of valuation
2. 2004 valuation results
3. Intervaluation experience
4. Results

HYMANS ROBERTSON

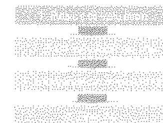
Purpose of triennial funding valuation



- Meet regulatory requirements
- Ensure "solvency" of the fund
- Determine rate at which employers will contribute over following 3 years

HYMANS ROBERTSON

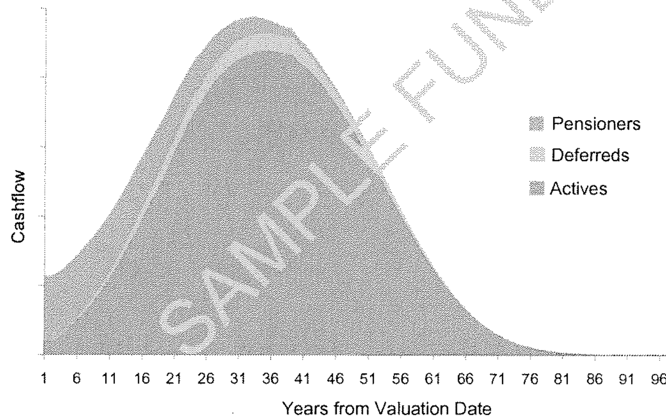
What is the pension fund?



- Defined benefit scheme
  - Member contributions fixed (for now!)
- Funded scheme
  - Assets built up to meet future benefit payments
- Future costs are uncertain

What is the pension fund?

Future Cash Flows (Past Service)



Source: Hymans Robertson LLP , sample client

Where were we?

2004 past service position

funding level : 69% whole fund

HYMANS ROBERTSON

2004 contribution requirement

	% of pay
Total cost of benefits	18.8%
Less: employee contributions	*6.0%*
Employer share of future service	12.8%
Plus: Adjustment for past service position	*10.1%*
Common Contribution Rate	22.9%

Deficit recovered over 20 years

HYMANS ROBERTSON

Stability at expense of margins

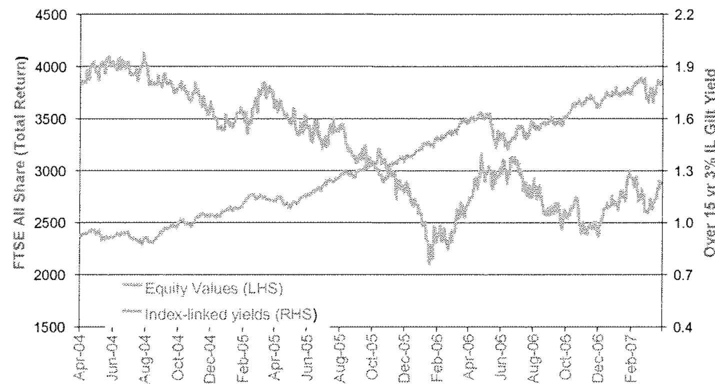
		Common Contribution Rate at 31/03/04 % of pay
2004 basis (1.6% AOA)		22.9%
Lower assumed asset out-perfomance on:		
Future service	2.1%	
Past service	2.1%	
		4.2%
Shorter deficit recovery		0.0%
2001 basis (1.25% AOA)		27.1%

No allowance for longevity improvements in 2004

HYMANS # ROBERTSON

Market conditions

Equity Returns and Gilt Yields

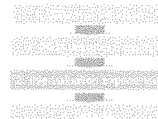


HYMANS # ROBERTSON

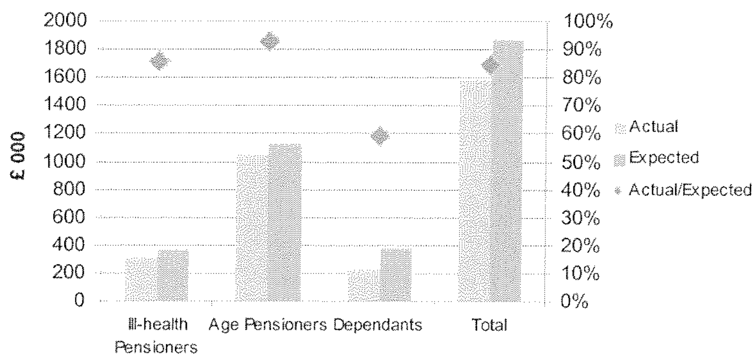
Benefit changes

- Principal changes (affecting valuation):
  - Rule of 85 re-introduced from April 2005
  - Commutation introduced from April 2006
  - Rule of 85 removed
    - for new entrants from October 2006
    - for existing members from 1 April 2008 (with protections)
- 2008 new scheme

Post-retirement mortality experience



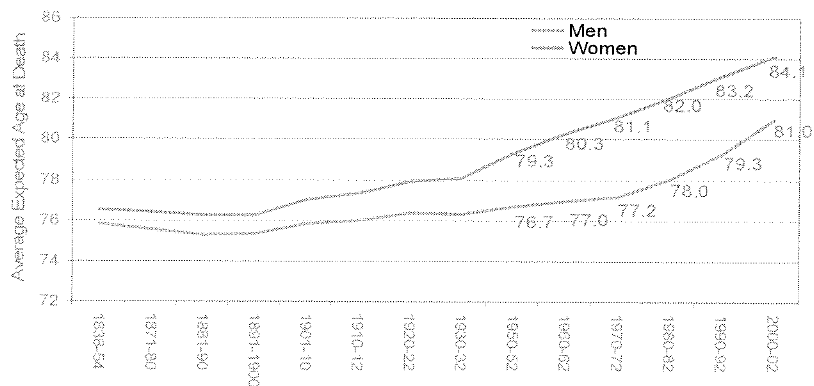
Actual v Expected Deaths (Amounts)



Mortality

1 year increase in life expectancy every decade

Life Expectancy at age 65: England and Wales



Source: Government Actuary, English Life Table series of mortality tables

HYMANS ROBERTSON

Results – Funding Level
Whole Fund

Valuation date	2004	2007
Past service liabilities	£m	£m
Employees	243	355
Deferred pensioners	102	154
Pensioners	243	290
Total liabilities	587	798
Assets	405	620
Surplus/(Deficit)	(182)	(178)
Funding Level	69%	78%

HYMANS ROBERTSON

Results – Funding Level
Haringey Council

Valuation date	2004	2007
Past service liabilities	£m	£m
Employees	223	273
Deferred pensioners	100	147
Pensioners	238	279
Total liabilities	562	699
Assets	385	521
Surplus/(Deficit)	(177)	(178)
Funding Level	69%	75%

HYMANS ROBERTSON

Results – Contribution rates Whole Fund

Valuation date	2004	2007
Future Service costs	% of pay	% of pay
Total cost	18.3%	20.6%
Employee conts	6.0%	6.7%
Expenses	0.5%	0.5%
Net employer share	12.8%	14.4%
Past service adj (20 yrs)	10.1%	7.2%
Common contribution rate	22.9%	21.5%

HYMANS ROBERTSON

Results – Contribution rates Haringey Council

Valuation date	2004	2007
Future Service costs	% of pay	% of pay
Total cost	18.2%	20.3%
Employee conts	6.0%	6.7%
Expenses	0.5%	0.5%
Net employer share	12.7%	14.1%
Past service adj (20 yrs)	10.2%	8.8%
Council contribution rate	22.9%	22.9%

HYMANS # ROBERTSON

Next steps

- Agree contribution rates and phasing
- Keep ill-health budgets under review
- Keep mortality experience under review
- Keep funding positions under review

…Valuation report signed off by 31 March 2008.

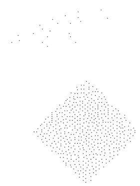
HYMANS # ROBERTSON

Future pressures

- Need to rebuild margins
- Future longevity improvements
- Benefit changes?

Still upward pressure on contribution rates

HYMANS ROBERTSON



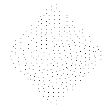
Any questions?

Real people. Real skills. Real results.

PUBLIC SECTOR

HYMANS ROBERTSON

Appendices



Real people. Real skills. Real results.

PUBLIC SECTOR

HYMANS ROBERTSON

Effect of market conditions

- Asset returns
  - Investment returns ☺
    - 13.1% p.a.
    - 6.3% p.a. more than discount rate of 6.3% p.a. (20% in total)
- Liabilities
  - Real gilt yields ☹
    - 1.8% p.a. to 1.3% p.a.
    - Liabilities up by c.12% (no change in strategy)

Overall – improvement in FL ☺

HYMANS ROBERTSON

Benefit changes

- Principal changes (affecting valuation):
  - Rule of 85 re-introduced from April 2005
  - Commutation introduced from April 2006
  - Rule of 85 removed
    - for new entrants from October 2006
    - for existing members from 1 April 2008 (with protections)
- Civil partnerships
- Anti-age discrimination changes
- Tax simplification

New scheme from 2008

- 1/60th member's pension, all cash by commutation
- 1/160th partners' pensions
- Two tier ill-health (3rd tier outside the scheme?)
- New DIS / IH service enhancements
- Higher lump sums on death
- Seven tier employee contributions
- Cost sharing to be considered in future

higher cost for existing members due to recycling

Commutation experience

- Analysis:
  - compare 3/80ths with new HMRC limit
  - all HR advised LGPS funds
  - number of members and weighted by pension amounts
- Initial experience analysis (FRS17)
  - 25% of members (amounts weighted)
- Assumed 50%
  - In line with GAD/ CLG assumptions
- Updated experience analysis
  - 15% of members (amounts weighted)

commutation reduces cost of existing scheme

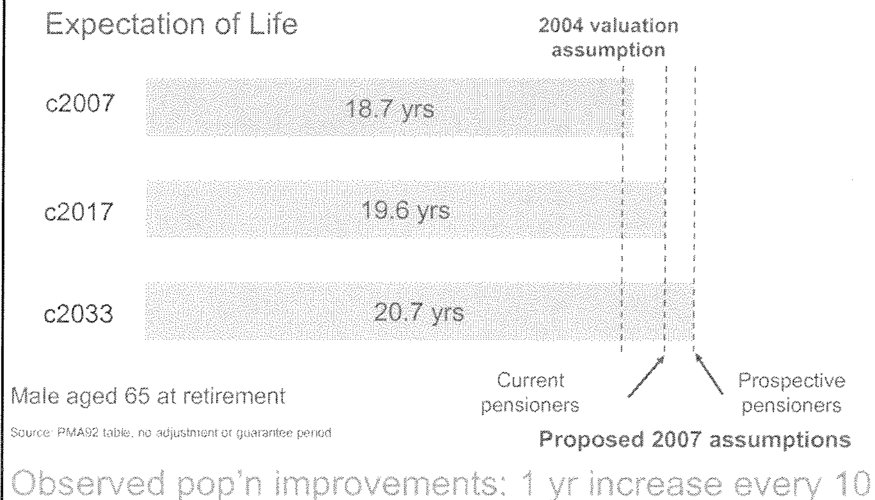
HYMANS ROBERTSON

Demographic assumptions

- No change in approach since 2004:
  - "best estimate" based on LGPS experience
- Refined to allow for 2001-04 experience
  - Fewer early leavers
  - Fewer ill-health early retirements
  - Commutation at 50%
- Specific consideration of future mortality improvements (no allowance in 2004)

HYMANS ROBERTSON

2007 Proposals



Observed pop'n improvements: 1 yr increase every 10

Pre-retirement experience

	Actual	Assumed
Early leavers	2,146	2,285
Ill health retirements	60	132
Salary increases *	4.9%	5.0%
Pension increases	3.1%	2.9%
Average age	50.1	49.1

* In respect of pre-98 full-time employees

Overall : reduction in funding level

APPENDIX TWO

1. Introduction

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

It has been revised 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 FSS and is effective from 31 March 2008.

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, or pools of employers, pay for their own liabilities.

The FSS forms part of a framework that includes:

- the Local Government Pension Scheme Regulations 1997 (regulations 76A and 77 are particularly relevant);
- the Rates and Adjustments Certificate, which can be found appended to 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.

1.2 Reviews of FSS

The FSS is reviewed in detail at least every three years ahead of triennial valuations being carried out, with the next full review due to be completed by 31 March 2011. 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 John Hardy in the first instance at john.hardy@haringey.gov.uk or on 020-8489-3726.

2. Purpose

2.1 Purpose of FSS

The **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.

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.

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 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.

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*[1], 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 of all the employers' scheme members.

The Fund's actuary is also required to adjust the Common Contribution Rate for circumstances which are deemed "peculiar" to an individual employer[2]. 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 or pool together with individual past service adjustments according to employer (or pool)-specific spreading and phasing periods.

Annex A contains a breakdown of each employer's contributions following the 2007 valuation for the financial years 2008/09, 2009/10 and 2010/11. It includes a reconciliation of each employer's rate with the *Common Contribution Rate*. It also identifies which employers' contributions have been pooled with others.

[1] See Regulation 77(4)
[2] See Regulation 77(6)

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.

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 and 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. 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 for improvements in line with PMA/PFA92 series projections up to calendar year 2017 for non-pensioners and 2033 for pensioners with age ratings applied to fit past LGPS experience. Employers are aware that their contributions are likely to increase in future if longevity exceeds the funding assumptions.

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 from the Fund's assets in excess of gilts or even match the return on 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.

Given the very long-term nature of the liabilities, a long term view of prospective returns from equities is taken. For the 2007 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. Based on the asset allocation of the Fund as at 31 March 2007, this is equivalent to taking credit for excess returns on equities of 2% p.a. over and above the gross redemptions yield on index-linked gilts on the valuation date and for excess returns of 0.4% p.a. on the non-equity assets

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

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 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.

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 2004 and 2007 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.

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 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.

Type of Employer	***Maximum* Length of Deficit Recovery Period**
Statutory bodies with tax raising powers	A period to be agreed with each employer not exceeding 20 years
Community Admission Bodies with funding guarantees	A period to be agreed with each employer subject to a maximum of the future working lifetime.
Best Value Admission Bodies	The period from the start of the revised contributions to the end of the employer's contract.
Community Admission Bodies that are closed to new entrants e.g. Bus Companies, whose admission agreements continue after last active member retires	A period equivalent to the expected future working lifetime of the remaining scheme members allowing for expected leavers, subject to not less than 9 years.
All other types of employer	A period 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.

The deficit recovery period starts at the commencement of the revised contribution rate (1 April 2008 for 2007 valuation). The Administering Authority would normally expect the same period to be used at successive triennial valuations, but would reserve the right to propose alternative spreading periods, for example, to improve the stability of contributions.

3.7.2 Surplus Spreading Periods

Any employers deemed to be in surplus may be permitted to reduce their contributions below the cost of accruing benefits, by spreading the surplus element over the maximum periods shown above (unless otherwise agreed by the Administering Authority and the Fund's actuary) for deficits in calculating their **minimum** contributions.

However, to help meet the stability requirement, employers may prefer not to take such reductions.

3.7.3 Phasing in of Contribution Rises

Best Value Admission Bodies are not eligible for phasing in of contribution rises. Other employers may opt to phase in contribution rises as follows:

- for employers contributing at or above its future service rate in 2007/08, phasing in the rise in employer contributions over a period of three years;
- for employers contributing at less than its future service rate in 2007/08, phasing in the rise in contribution rises over a period of three years.

3.7.4 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.

3.7.5 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 2004 valuation, or to phase-in contribution changes, will be assumed to incur a greater loss of investment returns on the deficit by opting to defer repayment. Thus, deferring paying contributions will lead to higher contributions in the long-term.

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

3.7.6 Pooled Contributions

The Administering Authority allows Haringey Council to pool the legacy liabilities and assets that remain when an employer leaves the Fund. Otherwise, the Administering Authority does not permit the pooling of contribution rates.

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.

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. This could give rise to significant payments being required.

(c) For Admission Bodies with guarantors, it is possible that any deficit could be transferred to the guarantor in which case it may be possible to simply transfer the former Admission Bodies members and assets to the guarantor, without needing to crystallise any deficit.

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

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 grounds of ill-health. All employers, irrespective of whether or not they are pooled, 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.

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 retirement 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.

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 2004, the proportion held in equities and property was 75.4% of the total Fund assets.

The investment strategy of lowest risk would be one which provides cashflows which replicate the expected benefit cashflows (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 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 funding policy currently adopts an asset outperformance assumption of 1.6% p.a. over and above the redemption yield on index-linked gilts. The Fund's investment strategy is detailed in our SIP. The Fund's Actuary considers that the funding basis does conform to the requirements to take a "prudent longer-term" approach to funding.

The Administering Authority is aware that, in the short term – such as the three yearly assessments at formal valuations – the proportion of the Fund invested in equities brings the possibility of considerable volatility and there is a material chance that in the short-term and even medium term, asset returns will fall short of the out-performance target. The stability measures described

in Section 3 will dampen 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. This process was informed by the use of Asset-Liability techniques to model the range of potential future solvency levels and contribution rates.

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's 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.

5.2 Financial Risks

Risk	Summary of Control Mechanisms
Fund assets fail to deliver returns in line with the anticipated returns underpinning valuation of liabilities over the long-term	*Only anticipate long-term return on a relatively prudent basis to reduce risk of under-performing.* *Analyse progress at three yearly valuations for all employers.* *Annual interim valuations.*
Inappropriate long-term investment strategy	*Set Fund-specific benchmark, informed by Asset-Liability modelling of liabilities.*
Fall in risk-free returns on Government bonds, leading to rise in value placed on liabilities	*Inter-valuation monitoring, as above.* *Some investment in bonds helps to mitigate this risk.*
Active investment manager under-performance relative to benchmark	*Short term (quarterly) investment monitoring analyses market performance and active managers relative to their index benchmark and target.*
Pay and price inflation significantly more than anticipated	*The focus of the actuarial valuation process is on real returns on assets, net of price and pay increases.*

	Inter-valuation monitoring, as above, gives early warning. *Some investment in index linked bonds also helps to mitigate this risk.* *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.*
Effect of possible increase in employer's contribution rate on service delivery and admission/scheduled bodies	*Seek feedback from employers on scope to absorb short-term contribution rises.* *Mitigate impact through deficit spreading and phasing in of contribution rises.*

5.3 Demographic Risks

Risk	Summary of Control Mechanisms
Ill-health retirements significantly more than anticipated.	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.
Pensioners living longer.	*Set mortality assumptions with some allowance for future increases in life expectancy.* *Fund actuary monitors combined experience of around 50 funds to look for early warnings of lower pension amounts ceasing than assumed in funding.*
Deteriorating patterns of early retirements	*Employers are charged the extra capital cost of non ill health retirements following each individual decision.* *Employer ill health retirement experience is monitored.*

5.4 Regulatory

<table>
<tr><th>Risk</th><th>Summary of Control Mechanisms</th></tr>
<tr><td>Changes to regulations, e.g. more favourable benefits package, potential new entrants to scheme, e.g. part-time employees</td><td rowspan="2">The Administering Authority is alert to the potential creation of additional liabilities and administrative difficulties for employers and itself.

The Administering Authority considers all consultation papers issued by the CLG and comments where appropriate.

The Administering Authority will consult employers where it considers that it is appropriate.</td></tr>
<tr><td>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</td></tr>
</table>

5.5 Governance

<table>
<tr><th>Risk</th><th>Summary of Control Mechanisms</th></tr>
<tr><td>Administering Authority unaware of structural changes in an employer's membership (e.g. large fall in employee members, large number of retirements).</td><td rowspan="2">The Actuary may be instructed to consider revising the rates and Adjustments certificate to increase an employer's contributions (under Regulation 78) between triennial valuations

Deficit contributions are expressed as monetary amounts and percentages (see Annex A).</td></tr>
<tr><td>Administering Authority not advised of an employer closing to new entrants.</td></tr>
<tr><td>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.</td><td>The Administering Authority requires employers with Best Value contractors to inform it of forthcoming changes.

It also operates a diary system to alert it to the forthcoming termination of Best Value Admission Agreements.</td></tr>
</table>

An employer ceasing to exist with insufficient funding or adequacy of a bond.	The Administering Authority believes that it would normally be too late to address the position if it was left to the time of departure. The risk is mitigated by: • *Seeking a funding guarantee from another scheme employer, or external body, where-ever possible.* • *Alerting the prospective employer to its obligations and encouraging it to take independent actuarial advice.* • *Vetting prospective employers before admission.* • *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.*

Annex A – Employers' Contributions, Spreading and Phasing Periods

Following the 2007 valuation, the minimum employer contributions shown in the Rates and Adjustment certificate attached to the 2007 valuation report are based on the deficit recovery periods and phasing periods shown in the table below. The table also shows the individual adjustments under Regulation 77(6) to each employer's contributions from the 'Common Contribution Rate'.

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 FSS and SIP, both after proper consultation with interested parties; and
- monitor all aspects of the fund's performance and funding and amend FSS/SIP
- 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; and
- notify the administering authorities 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 FSS; and

- prepare advice and calculations in connection with bulk transfers and individual benefit-related matters.