

# Agenda



**AGENDA for a meeting of the PENSIONS COMMITTEE to be held in COMMITTEE ROOM B, County Hall, Hertford on FRIDAY 18 NOVEMBER 2016 at 10.00AM**

## **MEMBERS OF THE COMMITTEE (10) - QUORUM 3**

C M Hayward (Chairman), R J Henry, J G L King, D E Lloyd, R G Parker, R Sangster, D T F Scudder, A M R Searing, A Stevenson, J D Williams (Vice-Chairman)

## **REPRESENTATIVES OF HERTFORDSHIRE DISTRICT / BOROUGH COUNCILS (3) (NON-VOTING)**

J Lloyd, K Ayling, M Freeman

### Invitees:

Colm O'Callaghan, District Finance Representative

Meetings of the Committee are open to the public (this includes the press) and attendance is welcomed. However, there may be occasions when the public are excluded from the meeting for particular items of business. Any such items would be taken at the end of the public part of the meeting and listed under "Part Two ('closed') agenda".

Committee Room B is fitted with an audio system to assist those with hearing impairment. Anyone who wishes to use this should contact main (front) reception.

## **PART I (PUBLIC) AGENDA**

### **1. MINUTES**

To confirm the minutes (Parts I and II) of the meeting held on 27 October 2016.

### **2. QUARTERLY RISK AND PERFORMANCE REPORT**

Report of the Director of Resources

### **3. FORMAL FUNDING VALUATION INITIAL RESULTS 2016**

Report of the Director of Resources

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**4. INVESTMENT STRATEGY REVIEW**

Report of the Director of Resources

**5. PENSION FUND ASSET POOLING –ACCESS UPDATE**

Report of the Director of Resources

**EXCLUSION OF PRESS AND PUBLIC**

The Chairman will move:-

*“That under Section 100(A)(4) of the Local Government Act 1972, the press and public be excluded from the meeting for the following item of business on the grounds that it involves the likely disclosure of exempt information as defined in paragraph 3 of Part 1 of Schedule 12A to the said Act and the public interest in maintaining the exemption outweighs the public interest in disclosing the information.”*

**PART II (‘CLOSED’) AGENDA**

**1. ANNUAL INVESTMENT MANAGER COSTS REPORT**

Report of the Assistant Director - Finance

**2. PENSION FUND - FUNDING & INVESTMENT REPORT (FORMERLY PERFORMANCE REPORT) AS AT 31 MARCH 2016**

Report of the Director of Resources

Appendix B to follow

**3. SWITCHING GLOBAL EQUITY MANAGERS**

Report of Mercer

**If you require further information about this agenda please contact Lisa Heaton, Democratic Services Officer, on telephone no (01992) 555456 or e-mail [lisa.heaton@hertfordshire.gov.uk](mailto:lisa.heaton@hertfordshire.gov.uk)**

Agenda documents are also available on the internet at:

<https://cmis.hertfordshire.gov.uk/hertfordshire/Calendarofcouncilmeetings.aspx>

*For further information about the issues covered in these reports please contact Patrick Towey on 01992 555148.*

# Minutes



To: All Members of the Pensions Committee

From: Legal, Democratic & Statutory Services  
Ask for: Lisa Heaton  
Ext: 25456

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## PENSIONS COMMITTEE 27 OCTOBER 2016

### ATTENDANCE

### MEMBERS OF THE PENSIONS COMMITTEE

E M Gordon (*substitution R J Henry*), C M Hayward (Chairman), J D Williams (Vice-Chairman), D E Lloyd, R G Parker, L F Reeve (*substitution J G L King*), R Sangster, D T F Scudder, A M R Searing, A Stevenson

### MEMBERS OF HERTFORDSHIRE DISTRICT/BOROUGH COUNCILS (2) NON VOTING

J Lloyd, M Freeman

Upon consideration of the agenda for the Pensions Committee meeting held on 27 October 2016 as circulated, copy annexed, conclusions were reached and are recorded below:

*Note: No conflicts of interest were declared by any member of the Cabinet Panel in relation to the matters on which conclusions were reached at this meeting.*

### PART I ('OPEN') BUSINESS

#### 1. MINUTES

- 1.1 A brief update was provided with regard to the ACCESS pooling delegation; it was noted that a letter was due to be sent to the Minister expressing concerns over committing further resources to the pool; however, Marcus Jones had since expressed his interest in meeting with representatives from each pool. A short update report would be provided at the November 2016 meeting.
- 1.2 The Minutes of the Cabinet Panel meeting held on 9 September 2016 were confirmed as a correct record and signed by the Chairman.

#### ACTION

CHAIRMAN'S  
INITIALS

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**2. DATES FUTURE MEETINGS**

Members noted the dates of future Pensions Committee meetings as follows:

- 18 November 2016 at 10.00am
- 24 February 2017 at 10.00am
- 31 March 2016 at 2.00pm
- 13 June 2016 at 10.00am

**KATHRYN PETTITT  
CHIEF LEGAL OFFICER**

**CHAIRMAN** \_\_\_\_\_

**CHAIRMAN'S  
INITIALS**

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## QUARTERLY RISK AND PERFORMANCE REPORT

### Report of the Director of Resources

Author of the report: Jolyon Adam, Finance Manager (Telephone: 01992 555078)

#### 1. Purpose of the Report

- 1.1 To provide the quarterly update on Risk and Performance for the Pension Fund for the period 1 July to 30 September 2016.

#### 2. Summary

- 2.1 The report provides an update on the following matters:

- Summary of reports to be presented to the December meeting of the Pensions Board;
- Current status of risk and governance matters that are monitored as part of the Risk Register;
- Current status of risk monitoring of Scheme Employers; and
- Performance of the Administering Authority measured against performance indicators set out in the Administration Strategy.

#### 3. Recommendation

That the Pensions Committee notes this report.

#### 4. Pension Board reports

- 4.1 The Pensions Committee is invited to note the following reports related to risk and performance that the Local Government Pension Scheme ( LGPS) and Fire Pension Boards (FPB's) will receive at their December and November meetings respectively:

##### LGPS Board

- **Risk and Governance Report (RGR)** providing a detailed quarterly update on the governance and management of the Pension Fund

- **London Pensions Fund Authority Administration Report (LPFA)** providing a quarterly update on the performance of the administration service for the Local Government Pensions Scheme

4.2 Pensions Boards have also committed to register and complete the Pensions Regulator’s on-line training in relation to Code of Practice 14, ‘Governance and Administration of Public Service Pension Schemes’, to further their understanding of relevant regulations and expectations of Board members

**Fire Board**

- **London Pensions Fund Authority Administration Report (LPFA)** providing a quarterly update on the performance of the administration service for the Firefighters’ Pension Scheme.
- **Internal Dispute Resolution Process (IDRP) Policy** outlining the policy relating to the processing and response to complaints and grievances submitted by members of the scheme.
- **Herts Fire & Rescue Service (HFRS) Pension Scheme Accounts & Annual Governance Report (AGR)** covering the period 1 April 2015 to 31 March 2016.
- **Risk Management Report** providing an overview of the key risks in relation to the HRFS.
- **Review of Operation of Pension Boards** providing an annual review of the activity and development of the Pension Board.

**5. Risk Register**

5.1 The Risk Register sets out risk control mechanisms that aim to either avoid or reduce the probability and/or impact of any risk event in relation to the Pension Fund. Risks are classified using the following criteria.

Risk Level	Description
<b>Severe</b>	The consequences will have a severe impact on the delivery of a key priority and comprehensive management action is required immediately.
<b>Significant</b>	The consequences of the risk materialising would be significant, but not severe. Some immediate action is required plus the development of an action plan.
<b>Material</b>	Consequences of the risk are not significant and can be managed through contingency plans. Action plans can be developed later to address the risk.
<b>Manageable</b>	Consequences of the risk are considered relatively unimportant. The status of the risk should be reviewed periodically.

5.2 Table 1 provides the risk current status of the four key risks and a summary of activities undertaken during the quarter to September 2016. The risk status key is shown in the following chart.

▲	An increase in risk status since the previous quarter
◀▶	Risk status has remained unchanged since the previous quarter
▼	A decrease in risk status since the previous quarter

**Table 1: Risk Register – Current Status and Activity Summary**

Risk	Risk Level	Change in Risk Status	Quarterly Activity Summary
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A	The Pension Fund Investment Strategy does not deliver the long term projected investments returns and does not comply with legislation.	<b>Amber</b>	◀▶	<p>Government approval of ACCESS pooling submission is still awaited. The Minister for Local Government has requested to meet with ACCESS representatives in November to discuss the submission. A separate report on the current activity around ACCESS pooling is being presented to this meeting.</p> <p>A separate paper on Investment Strategy is being presented to this meeting of the Pensions Committee which will outline the proposal for reviewing and producing a revised Strategy which will take effect from April 2017.</p>
B	The funding level of the Pension Fund deteriorates.	<b>Amber</b>	◀▶	<p>Initial whole fund results are now available and will be presented to the Committee as a separate item on this agenda.</p> <p>Individual employer's results will be circulated in late November/early December.</p> <p>All Parish &amp; Town Councils have now responded to the consultation that closed in May 2016 with the final outstanding council choosing to remain in the pool. The pool will remain active for the following valuation period and will be reviewed at the 2019 Triennial Valuation.</p>
C	Scheme employers default on meeting their obligations to the Pension Fund and LGPS.	<b>Amber</b>	◀▶	<p>A risk based approach has been adopted for the 2016 valuation with scheme employers categorised as low, medium or high risk determined by a number of factors including the strength of their covenant. This rating will be used to set the funding targets for each scheme employer given a minimum level of probability.</p> <p>Validation checks on membership data have been carried out as part of the 2015/16 Annual Benefit Statement exercise and 2016 Valuation.</p>
D	The Pension Fund and its third party providers do not comply with regulations, statute or	<b>Green</b>	◀▶	Hertfordshire is acting as lead administering authority for the procurement of legal advice for the



	procedure.		ACCESS pool. Tender documentation is in the process of being drafted to secure a resource for the pool which will support with the legal considerations involved with planning and procurement of the operator of the Collective Investment Vehicle (CIV).
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## 6. Scheme Employers Risk Monitor

6.1 Scheme Employers are monitored on a monthly basis to measure the trend and current status of risk where scheme employers' covenants may have a detrimental impact on the Pension Fund.

6.2 Scheme employers are rated as:

- **RED - high risk:** This indicates that action is required to mitigate the risks to the Pension Fund where there is a high risk of a scheme employer defaulting on its obligations to the Pension Fund.
- **AMBER - medium risk:** This indicates that scheme employers require review or ongoing monitoring to determine whether any actions need to be taken to mitigate the risks identified.
- **GREEN - low risk:** This indicates that there are no immediate issues or actions to be taken.

Table 2 provides a summary of the current position, with comparative data for previous quarters.

**Table 2: Employer Risk Monitor – Current Trend and Status**

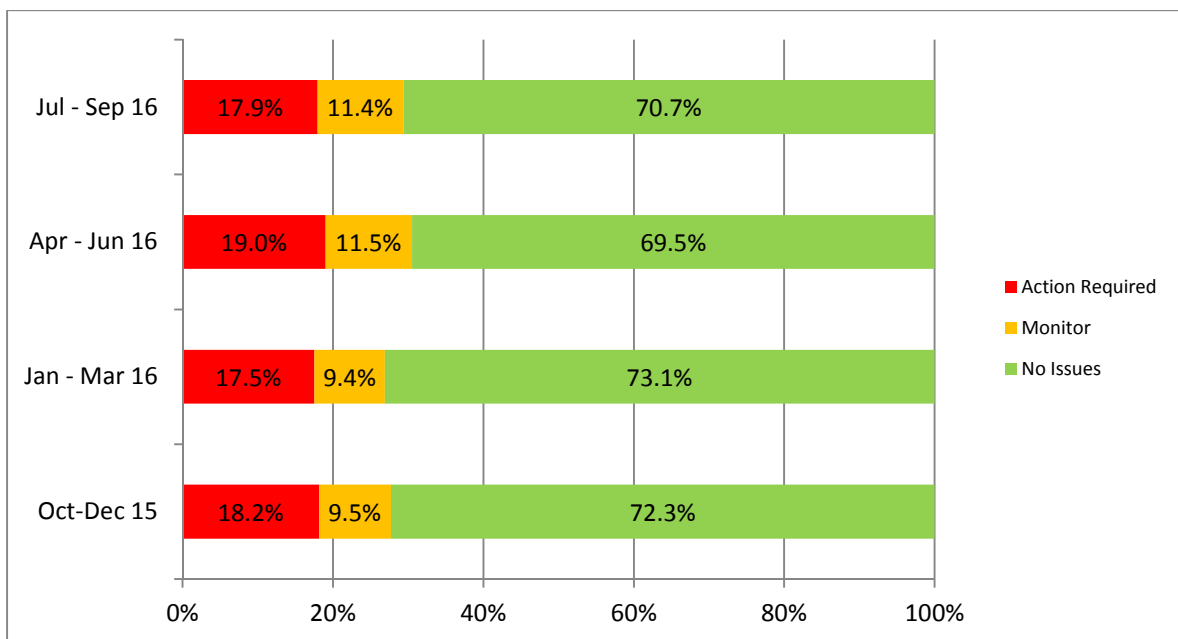


Table 3 provides an analysis of the number of scheme employers in each risk category together with the value of net liabilities (based on the 2013 Valuation) for each risk category with a comparison to the previous quarter.




**Table 3: Analysis of Scheme Employers by Risk Category**

April – June 2016				Risk Category	July – September 2016			
Scheme Employers		Net Liabilities			Scheme Employers		Net Liabilities	
No.	%	£ m	%		No.	%	£ m	%
66	19.0	14.5	2.4	<b>Red</b>	63	17.9	14.4	2.3
40	11.5	87.1	14.1	<b>Amber</b>	40	11.4	87.1	14.1
242	69.5	515.4	83.5	<b>Green</b>	248	70.7	515.5	83.6
<b>348</b>	<b>100.0</b>	<b>617.0</b>	<b>100.0</b>	<b>Total</b>	<b>351</b>	<b>100.0</b>	<b>617.0</b>	<b>100.0</b>



## 7. Administering Authority Performance Monitoring



7.1 The performance of the Administering Authority and scheme employers in managing and administering the Pension Fund is measured against performance indicators set out in the Administration Strategy. This section also includes information about treasury management performance against the annual Treasury Management Strategy.




7.2 Table 4 provides the current status and commentary on the performance indicators. The performance status key is shown in the following chart.

	A deterioration in performance since the previous quarter
	Performance has remained unchanged since the previous quarter
	An improvement in performance since the previous quarter

**Table 4: Administering Authority Performance Monitor**

Indicator	Change in Performance Status	Commentary
Audit Reviews		Work will shortly commence on the Internal Audit of Pensions Administration as outlined in the 2016/17 Shared Internal Audit Service (SIAS) Audit Plan. This is currently scheduled to commence during Q3.
Complaints and Internal Disputes		During the quarter there were two new LPFA service complaints, compared to one in the last quarter. Both of these complaints were resolved within the quarter.  One related to tax deductions on a significant pension payment. The individual's pension was due to go into payment 18 months previously, but the completed forms were only recently received. This resulted in 18 months of arrears being paid within the first payment, and a subsequent deduction of a large amount of tax. LPFA advised the member to contact HMRC to resolve this as they would not speak to LPFA

		<p>regarding individual member's affairs.</p> <p>The second complaint was regarding the transfer of a member's benefits from Enfield Borough Council. Despite repeated chasers Enfield had not been timely in providing required information due to changes in recent changes in regulations and Government Actuary's Department (GAD) factors. The information has now been received and the complaint closed.</p> <p>During the quarter to 30 September 2016 two IDRPs were raised against the Administering Authority, and one carried forward IDRPs was responded to.</p> <p>Both new IDRPs related to members challenging the reduction of their pension following Guaranteed Minimum Pension (GMP) reconciliation.</p> <p>The carried forward IDRPs related to the implementation of a Pension Sharing Order (PSO) following divorce proceedings, and an overpayment of pension which had occurred between this order being put in place, and the changes to the member's pension record being effected by the LPFA. Overpayments commonly occur in cases where pension is already in payment - which have to be subsequently reclaimed - and the IDRPs was dismissed as statutory timescales were met.</p>
Scheme Employer Late Payments and Penalty Charges		<p>There were 13 penalty charges raised for the period to 30 June 2016 against 12 scheme employers for late payment of contributions or late return of monthly contribution forms.</p> <p>Details are provided in the LPFA's quarterly Administration Report presented to the Pensions Board.</p>
LPFA Administration Service Performance Indicators		<p>Officers are working with the LPFA to address the backlog of Defined Benefit cases, and develop the action plan already in place to continue to reduce this backlog in light of the one-off increases arising from year-end processes.</p> <p>Recruitment is underway to replace leavers and a project plan is being maintained to clear the backlog of cases.</p>
Treasury Management		<p>The average size of the portfolio at 30 September 2016 was £12.2m increasing from £9.3m in the previous quarter. This is below the cap of £35m.</p> <p>Interest earned in the quarter to 30 September 2016 was £11.9k increasing from £11.3k in the previous quarter.</p>

	    	<p>The rate of return was 0.39% decreasing from 0.49% in the previous quarter. This was 0.19% above the benchmark of the average 7 day London Interbank Bid (LIBID) rate of 0.20%</p> <p>There was a breach of the Pensions Fund's Treasury Management Strategy on 19 September 2016 due to a failure of the Barclays.net online banking system. The failure of this system prevented the Council's Treasury Team from making any outward payments, therefore making it impossible to place deals and transfer funds to investments on that date. As a result, the Pensions fund breached its counterparty limit with Barclays of £3.5m, as £6.9m was held in the Barclays current account overnight.</p> <p>Barclays have acknowledged full responsibility for this breach, agreed to pay compensation for lost interest, and reviewed their contingency processes for alternate payment mechanisms in the event of future possible failures of Barclays.net.</p>
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**FORMAL FUNDING VALUATION INITIAL RESULTS 2016**

*Report of the Director of Resources*

Author of the report: Patrick Towey, Head of Specialist Accounting (Telephone: 01992 555148)

**1. Purpose of the Report**

- 1.1 To provide the Pensions Committee with the initial results of the formal valuation of the Hertfordshire Pension Fund at 31 March 2016.
- 1.2 To recommend the approach for the review, consultation and final approval of the Funding Strategy Statement (FSS)

**2. Summary**

- 2.1 The Hertfordshire Pension Fund is formally valued by the Fund's actuary Hymans Robertson every three years, triennial valuation. The Fund when last valued at 31 March 2013 was valued at 82%. The report attached as Appendix A, shows the initial results for the valuation at the 31<sup>st</sup> March 2016. The interim results show that the funding level at 31 March 2013 was valued at 91%. Please note that these results are whole Fund results and that individual employer results including employer contribution rates will be issued from November. Individual employer results will also report different funding levels due to the nature of the characteristics of their member profiles, cash flows, and funding level at the last valuation.
- 2.2 As part of the Valuation process the Administering Authority is required to prepare a Funding Strategy Statement (FSS). The FSS is prepared every three years in collaboration with the Fund's actuary Hymans and after consultation with the Fund's employers. The FSS must be agreed and approved by the 31 March 2017.

**3. Recommendations**

- 3.1 That the Pensions Committee notes
  - (i) the initial results of the 2016 formal Funding valuation; and
  - (ii) the process for the review of the Funding Strategy Statement, consultation with employer bodies and final agreement by the Pension Committee at its meeting on 24 February 2017

#### 4. Initial Valuation results

- 4.1 The Local Government Pension Scheme (LGPS) regulations require that a formal valuation of the Fund takes place every three years, known as the triennial valuation. The report attached as Appendix A sets out the initial results for the Fund as a whole. The main headline to report to this Committee is that there has been an overall improvement in the Funding level of the Fund and a reduction in the reported Fund deficit; this is a very positive result for the Hertfordshire Fund. The table below compares the Funding level and deficit position for the Fund at 31 March 2013 and at 31 March 2016.

Valuation Date	Funding Level (%)	Surplus/Deficit (£m)
31 March 2013	82	(617)
31 March 2016	91	(336)

- 4.2 As part of the valuation process the actuary will agree with the Administering Authority (AA) a set of assumptions for investment returns, gilts and inflation, and membership experience. The investment consultant Mercer will also take part in this conversation particularly when setting the assumption for asset out performance i.e. investment return. The results set out in the Appendix compare the actual experience against the assumptions agreed with the actuary back in 2013. The actuarial assumptions for this valuation were agreed by this Committee at its meeting on 10 June 2016.

#### 4.3 Investment experience

For the period 2013 to 2016 the actual investment experience for the Hertfordshire Fund was greater than the assumption set by the actuary and AA, this was a positive contribution for the Fund.

Investment returns	Expected	Actual	Difference
Over 3 years	15.1%	22.2%	7.1%

#### 4.4 Gilts and inflation

The fall in gilt yields during the period which is used as part of the discount rate to discount liabilities had a negative impact on the Fund in that it increased the value of the liabilities. Actual inflation experience during the period was better than assumed and was another positive contribution to the funding value.

Assumption/measure	2013	2016	Difference
Long-dated gilt yields p.a.	3.0%	2.2%	(0.8%)
Expected inflation	3.3%	3.2%	(0.1%)

#### 4.5 Membership experience

Membership experience during the period was overall a positive contribution to the improvement in funding level in that there were fewer ill health and early retirements than assumed. Salary and benefits increases were also less than assumed. However, the number of pensions in payment ceasing was less than than expected which reflects the improvement in life expectancy but increases the liability on the fund.

4.6 In summary, although the liability position has increased over this period the assets have also increased and at a faster rate than the liabilities which is illustrated in the table below.

Valuation date	31 March 2013	31 March 2016
Liabilities	£3,525m	£3,920m
Assets	£2,908m	£3,584m
Surplus/(Deficit)	(£617m)	(£336m)
Funding level	82%	91%

#### 5. Scheme Advisory Board results

5.1 The Fund's actuary is also now required to submit valuation results to the Scheme Advisory Board (SAB) which are based on common assumptions issued by the Government Actuary Department (GAD). This allows the SAB and GAD to compare Funds on a like for like basis. Based on the assumptions used by GAD, the funding level of the Hertfordshire Fund is 107%, the results reported by GAD so far (28 out of 89 LGPS Funds) show a range from between 78% to 123% in funding levels. The Hertfordshire Fund is in the top 5 of reported funds.

#### 6. Funding Strategy Statement

6.1 Administering Authorities are required to maintain and publish a Funding Strategy Statement (FSS), the FSS is a summary of the Fund's approach to funding its liabilities, and this includes reference to the Fund's other policies such as the Statement of Investment Principle (Investment Strategy Statement wef. 1 April 2017). It is a regulatory requirement for each Fund to have a FSS and it is reviewed every three years during the valuation process. The FSS applies to all employer bodies participating in the Fund. The draft FSS, attached as Appendix B, has been prepared in conjunction with the scheme actuary, Hymans and sets out how the Administering Authority has balanced the conflicting aims of:

- Affordability of employer contributions;
- Transparency of processes;
- Stability of employers' contributions; and
- Prudence in the funding basis.

- 6.2 The FSS focuses on how employer liabilities are measured, the pace at which these liabilities are funded, and how employers or pools of employers pay for their own liabilities. The pension benefits accrued by employees by their participation in the LGPS are guaranteed by the LGPS regulations, and do not change with market values or employer contributions. Investment returns will help pay for some of the benefits, but probably not all, and certainly with no guarantee. The balance for the payment of accrued and future benefits is met by employee and employer contributions. The contributions made by employees are fixed under the regulations and therefore, the employers need to pay the balance of the cost of delivering the benefits to members and their families. The FSS is the framework within which the Fund's actuary carries out triennial valuations to set employers' contributions and provides recommendations to the Administering Authority when other funding decisions are required, such as when employers join or leave the Fund.
- 6.3 As part of the review process of the FSS, this document will also go to the Pension Board for review and comment and is then circulated to all scheme employers for a short consultation period. Following this review and consultation, the revised FSS will come back to the Pension Committee for final approval at its meeting on 24 February 2017.



# 2016 Formal Funding Valuation Initial Results

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APPENDIX A

Hertfordshire County Council Pension Fund



Barry McKay

Julie West

For and on behalf of Hymans Robertson LLP

6 October 2016

HYMANS ROBERTSON LLP

## Executive Summary

### Initial results

The initial draft whole fund results of the valuation are set out below based on your agreed funding basis: The results at the 2013 formal valuation are shown for comparison.

Valuation Date	31 March 2013	31 March 2016
<b>Past Service Liabilities</b>	<b>(£m)</b>	<b>(£m)</b>
Employees	1,277	1,279
Deferred Pensioners	690	873
Pensioners	1,558	1,768
<b>Total Liabilities</b>	<b>3,525</b>	<b>3,920</b>
<b>Assets</b>	<b>2,908</b>	<b>3,584</b>
<b>Surplus / (Deficit)</b>	<b>(617)</b>	<b>(336)</b>
<b>Funding Level</b>	<b>82%</b>	<b>91%</b>

### Assumptions

The key financial and demographic assumptions agreed and adopted for the 2016 valuation are set out below:

	31 March 2013	31 March 2016
Financial		
Discount rate	4.8%	4.0%
Benefit increases	2.5%	2.1%
Salary increases	3.8%	2.2%
Demographic		
Baseline Longevity	Club Vita	Club Vita
Future Improvements	CMI2010, Peaked, 1.25% p.a. long term	CMI2013, Peaked, 1.25% p.a. long term

### Solvency

The funding level on your agreed funding basis has improved from 82% in 2013 to 91% in 2016. Additionally, the funding deficit has decreased. The main reasons for the change in the funding level over the period were better than anticipated investment returns, deficit contributions and positive membership experience.

### Contribution rates

Every employer has their own tailored funding plan and valuation results will vary depending on their own membership, funding plan and experience since the last valuation (or since they joined the Fund). The change in the financial assumptions will put upward, on the cost of future service, however, positive membership experience should help to reduce deficit contributions. However, each employer will have a contribution rate calculated which will be dependent on their timeframe in the Fund and their risk categorisation. This will mean changes in contribution rates will vary by employer as we develop more bespoke contribution strategies.

### Next steps

The purpose of this report is to present the initial whole fund solvency results and summarise the experience over the intervalation period. This report is useful to identify any areas of potential risk that the Fund may want to consider and explore possible avenues of risk mitigation during the valuation process.

The next milestone in the valuation process is preparation of the draft individual employer results.

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## 1. Introduction

We have been commissioned by Hertfordshire County Council (“the Administering Authority”) to carry out a full actuarial valuation of the Hertfordshire County Council Pension Fund (“the Fund”) as at 31 March 2016 as required under Regulation 62 of the Local Government Pension Scheme Regulations 2013 (“the Regulations”). This report has been prepared to communicate the initial results of the 2016 valuation at whole fund level. It sets out the following:

- an analysis of Fund experience over the valuation period;
- your agreed funding assumptions;
- whole Fund valuation results; and
- analysis to help inform the Fund’s understanding of its risk exposure.

This report is addressed to Hertfordshire County Council in its role as Administering Authority to the Hertfordshire County Council Pension Fund. It should not be shared with any third parties without our prior written consent. Where consent is given, the report should be supplied in full including any related reliances and limitations.

Please note that Hymans Robertson LLP accept no liability to any third parties. The reliances and limitations in the body and appendices of this report apply equally to all users of this report.

## 2. Intervaluation Experience

Since the previous valuation, various events have taken place which affect the funding position of the Fund.

Investment returns	Expected	Actual	Difference	Impact
Over 3 year period	15.1%	22.2%	7.1%	Positive
Annual	4.8%	6.9%	2.1%	Positive

Assumption/measure	2013	2016	Difference	Impact
Long-dated gilt yields (p.a.)	3.0%	2.2%	(0.8%)	Negative
Expected inflation	3.3%	3.2%	(0.1%)	Positive

### Investment returns

The Fund has experienced better than anticipated investment returns. The return in excess of the 2013 valuation discount rate serves to ‘pay back’ a greater portion of the deficit than expected (all other things being equal). Therefore, all other things being equal, this improves the funding position. Investment returns in excess of discount rate were anticipated when setting contributions for some employers at the last valuation.

### Gilts and inflation

There has been a significant drop in gilt yields over the inter-valuation period which is reflected in a reduction in anticipated investment returns and therefore a reduction in the discount rate used to place a value on the liabilities. This increases the liabilities and puts upwards pressure on employer contribution rates.

Long term expectations for Retail Prices Inflation (RPI) and Consumer Price Inflation (CPI) have fallen slightly since 2013. This will offset some of the increases caused by the fall in gilt yields.

### Fund expenses

The Fund’s expenses (in relation to non-investment activities) over the last 3 years have totalled £7.046m. This figure is equivalent to 0.5% when expressed as a percentage of pensionable pay and an allowance for 0.4% was made at the last valuation. Unless otherwise instructed, we propose to make allowance for the Fund’s expenses by adding an allowance of 0.5% of pay to employer contribution rates payable from 1 April 2017.

### Membership experience

The areas of membership experience that have had the greatest effect on the results of the valuation are set out below:

	Expected	Actual	Difference	Impact
<b>Pre-retirement experience</b>				
Early leavers (no.of lives)	15,323	14,084	(1,239)	Positive
Ill-health retirements* (no.of lives)	369	171	(198)	Positive
Salary increases (p.a.)	4.3%	2.8%	(1.5%)	Positive
<b>Post-retirement experience</b>				
Benefit increases (p.a.)	2.5%	1.3%	(1.2%)	Positive
Pensions ceasing (£m)	8.3	8.0	(0.3)	Negative

\*Tier1 and Tier 2 ill-health retirements only

The impact of fewer members withdrawing than expected depends on the age and liability distribution of withdrawing members. Although in number terms there were fewer withdrawals than expected, the impact on the funding position was slightly positive for the Fund as there were more leavers than expected at older ages (where members will have greater liabilities).

The pensioner mortality experience has been very close to expectations due to the Fund’s use of Club Vita to inform the longevity assumption.

Membership experience overall has been positive over the intervaluation period. The most significant items of experience to note are:

- Salary increases have been less than assumed;

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- Pension increases have been less than assumed;
- Ill-health retirements have been slightly less than assumed; and
- 50/50 take-up has been significantly lower than expected.

**Regulatory experience**

The Fund is subject to risks beyond its control. In particular, since 2013:

- A new benefit structure has come into force;
- Funds have come under greater scrutiny from the Government Actuary's Department, the Scheme Advisory Board and the Department for Communities and Local Government (DCLG); and
- Cost controls may alter member benefits (but will have no effect on the 2016 valuation).

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### 3. Data and Assumptions

#### Data

We have relied on the data provided by the Administering Authority when carrying out our calculations. The accuracy of our results is limited by the quality of the data provided. We have carried out validations on the data provided to ensure it is fit for the purpose of the valuation. Further details can be found in our paper entitled “Data report for 2016 valuation”, which will follow shortly. We believe the membership data is of a good standard and is fit for the purposes of this valuation.

#### Financial assumptions

Your agreed financial assumptions are set out below, along with the assumptions adopted for the 2013 formal valuation:

Financial assumptions	31 March 2013	31 March 2016
Discount rate		
Return on long-dated gilts	3.0%	2.2%
Asset Outperformance Assumption	1.8%**	1.8%***
<b>Discount rate</b>	<b>4.8%</b>	<b>4.0%</b>
Benefit increases		
Retail Prices Inflation (RPI)	3.3%	3.2%
Assumed RPI/CPI* gap	(0.8%)**	(1.0%)**
<b>Benefit increase assumption (CPI)</b>	<b>2.5%</b>	<b>2.1%</b>
Salary increases		
Retail Prices Inflation (RPI)	3.3%	3.2%
Increases in excess of RPI	0.5%**	(0.9%)**
<b>Salary increase assumption</b>	<b>3.8%</b>	<b>2.2%</b>

\* Consumer Prices Index

\*\* Arithmetic addition

\*\*\* Geometric addition

#### Longevity assumptions

Your agreed longevity assumptions result in the following typical future life expectancies from age 65 (figures for 2013 shown for comparison):

	31 March 2013	31 March 2016
Male		
Pensioners	22.3 years	22.5 years
Non-pensioners	24.3 years	24.1 years
Female		
Pensioners	24.5 years	24.9 years
Non-pensioners	26.7 years	26.7 years

*Non-pensioners are assumed to be aged 45 at 31 March 2016*

#### Additional assumptions

##### Retirement age pattern

We have adopted the retirement age pattern assumption as specified by the Scheme Advisory Board for preparing Key Performance Indicators. Further details about this assumption are available on request.

##### 50/50 option

Following analysis of both the Fund’s actual take up rate, and national statistics, the Fund has assumed that 2% of members will take up the 50/50 option in the future.

##### Other assumptions

All other assumptions have been updated to reflect the latest experience of LGPS funds. Further details regarding the assumptions adopted are set out in the 2016 valuation toolkit and were agreed by Pensions Committee following presentation of our paper “2016 Formal Valuation: Setting the Funding Target” dated 23 May 2016.

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## 4. Initial Results - Solvency

The solvency of the Fund as at 31 March 2016 based on your agreed assumptions is set out below. The results at the 2013 formal valuation are shown for comparison.

Valuation Date	31 March 2013	31 March 2016
<b>Past Service Liabilities</b>	<b>(£m)</b>	<b>(£m)</b>
Employees	1,277	1,279
Deferred Pensioners	690	873
Pensioners	1,558	1,768
<b>Total Liabilities</b>	<b>3,525</b>	<b>3,920</b>
<b>Assets</b>	<b>2,908</b>	<b>3,584</b>
<b>Surplus / (Deficit)</b>	<b>(617)</b>	<b>(336)</b>
<b>Funding Level</b>	<b>82%</b>	<b>91%</b>

We have valued the benefits defined under the Regulations based on the assumptions outlined earlier. These results are sensitive to the underlying financial and demographic assumptions as well as the quality of the underlying data.

### Liabilities

The liabilities have grown substantially since 2013 mainly as a result of the change in the financial assumptions. The change in the net discount rate (essentially the difference between the discount rate and the assumed rates of increase of salaries, deferred pension revaluation or pensions in payment) results in a higher value being placed on the liabilities.

### Assets

The assets have also grown substantially over the inter-valuation period. This is a result of much better than assumed asset returns. This strong investment return has more than offset the increase in liabilities.

### Funding level/deficit

The overall result has been an improvement in the reported funding level of the Fund alongside a reduction in the funding deficit.

### Analysis of change in solvency

The table below illustrates the various factors that have led to the change in funding position between the 2013 and 2016 valuations.

Analysis	(£m)	
<b>Surplus / (deficit) at 31 March 2013</b>		<b>(617)</b>
Interest on surplus / (deficit)	(93)	
Investment returns greater than expected	209	
Contributions greater than cost of accrual	99	
Membership experience over the period	163	
Change in demographic assumptions	9	
Change in mortality assumption	37	
Change in financial assumptions	(179)	
Impact of LGPS 50/50 take up	(21)	
Other experience items	57	
<b>Surplus / (deficit) at 31 March 2016</b>		<b>(336)</b>

### Comment on employers

Every employer is valued separately based on their own membership data as part of the valuation and their change in funding position will therefore vary compared to that of the whole fund.

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## 5. Initial Results – Contributions

### Changes to terminology

The Regulations have introduced new terminology in respect of contribution rates. We have set out our interpretation of these terms below based on CIPFA guidance on preparing a Funding Strategy Statement.

### Primary Contribution Rate

This refers to the cost of new benefits being earned by members. This was previously referred to as the Future Service Rate.

### Secondary Contribution Rate

This refers to the contributions required to repair an employer's deficit (surplus). This was previously referred to as Deficit Recovery Contributions.

### Common Contribution Rate

The Regulations no longer require the reporting of the Common (Whole Fund) Contribution Rate. This has been replaced by Whole Fund Primary and Secondary Contribution Rates calculated as the payroll weighted average of the Primary and Secondary Contribution Rates for employer. These rates will be calculated and disclosed in the final valuation report.

### Typical employer results

The fall in the net discount rate will place upwards pressure on primary contribution rates. Employer deficit results are more difficult to predict due to the variable changes in funding levels. Therefore, we anticipate for most employers that there will be upward but manageable pressure on employer contribution rates for the majority of employers in the Fund.

### Employer categorisation

Every employer in the Fund is different. For instance, they have different funding levels, sources of funds for paying contributions, covenants, maturity profiles, and timeframes for their participation in the Fund.

As a result, when setting contribution rates, employers are categorised based on their individual characteristics in order to build a credible funding plan that fits their own needs while recognising the risk they pose the Fund and other participating employers.

### Setting credible funding plans

#### Set a funding target

For the vast majority of employers, the target is to be fully funded on the Fund's ongoing funding assumptions. There may be instances where alternative assumptions are used such as where an employer is approaching cessation.

#### Choosing an appropriate time horizon

Once a target has been chosen, the time employers are given to reach that target needs to be determined. For long-term secure employers, this is up to 20 years. For employers that pose a greater risk to the Fund, this may be much shorter. In general, a shorter time horizon results in more volatile contributions compared to employers with longer time horizons.

#### Probability of reaching the target

The final stage involves determining the probability required for each employer to reach its funding target within its time horizon. In general, higher probabilities of success are achieved by paying higher contributions and relying less on volatile investment returns. The probability required of each employer is largely based on each employer's assessed covenant. For instance, a lower probability of success (e.g. 66%) may be required for a secure body as they may be considered to be able to pay higher contributions (or current rates for longer) should they not reach their funding target over their time horizon.



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## 6. Risk Analysis

The valuation results depend critically on the actuarial assumptions that are made about the future of the Fund. If all of the assumptions made at this valuation were exactly borne out in practice then the results presented in this document would represent the true cost of providing benefits from the Fund as it currently stands at 31 March 2016.

However, no one can predict the future with certainty and future experience will not exactly match all of our assumptions. The future therefore presents a variety of risks to the Fund which should be **identified** and, where possible, the financial significance should be **quantified**. Thereafter the Fund can assess how (or if) these risks can then be **controlled** or **mitigated** and put in place **monitoring** to assess whether any mitigation is actually working.

### Financial risks

The two main areas of financial risk of interest to your Fund are the investment performance and level of benefit increases. To help understand the impact of these two factors being different from assumed, we have shown the effects on the solvency measure of varying the discount rate (investment performance) and benefit increase assumptions below.

Benefit Increases					
Discount Rates		1.9%	2.1%	2.3%	
	4.2%	(114)	(224)	(338)	(Deficit)
		97%	94%	91%	Funding Level
	4.0%	(222)	(336)	(453)	(Deficit)
	94%	91%	89%	Funding Level	
3.8%	(334)	(451)	(572)	(Deficit)	
	91%	89%	86%	Funding Level	

The above analysis focuses on financial risk to the solvency level. Our approach to setting contribution rates at the 2016 valuation seeks to recognise

the uncertainty around future investment returns and benefit increases. Further information about this method will be present with the employer results.

### Demographic assumptions

The main area of demographic risk is people living longer than expected. We have shown below the high level impact of people living longer than currently expected by using a more prudent assumption for future longevity improvements. The more prudent assumption assumes that the rate of future improvements continues to increase ('non-peaked'). The valuation assumption assumes that the rate of future improvements have peaked.

	Peaked improvements	Non-peaked improvements
(Deficit)	(336)	(425)
Funding Level	91%	89%

### Other risks to consider

There are other risk factors which would have an impact on the funding position. Examples of these include the level of ill health retirements, withdrawals from the scheme and take up of the 50:50 option. These are probably unlikely to change in such a way that would rank them as amongst the highest risks facing the Fund and therefore we have not sought to provide further quantification of their risk.

### Other events

Since carrying out the valuation, the United Kingdom held a referendum on its participation as a full member of the European Union. The result was a mandate to leave the European Union. At this time, it is difficult to predict the long term effect of this possible course of action. We have made no allowance for the referendum result in preparing this report.

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## 7. Next Steps

The purpose of this report is to present the initial whole fund solvency results and summarise the experience over the intervaluation period. This report is useful to identify any areas of potential risk that the Fund may want to consider and explore possible avenues of risk mitigation during the valuation process.

The next steps in the process are as follows.

- All parties to **understand the whole fund results** and the assumptions on which they are based, discuss any questions or issues before moving on to the next stage of the valuation process. This includes the Fund **identifying any areas of risk** that it is concerned about and wishes to explore further and understand how the risk can be identified, quantified, mitigated and monitored.
- Once all parties are happy with the whole fund results, we will quantify the **valuation results for each individual employer** that participates in the Fund. When we present you with these results, we will set out the contribution rates that each employer should pay for the next three years from 1 April 2017 based on the funding principles previously discussed.
- For some employers, the contribution rate that they should pay in principle may be different to what they will actually pay in practice. Any deviation will be based on their own circumstances and a range of factors including (amongst other things) their perceived security, whether they are going to be pooled with other employers or any budgetary constraints that they may be bound by. We expect there to be a consultation period where you gather together all of these issues and **come back to us with a set of final agreed contribution rates for each employer**.
- We understand that you may require additional input from us before agreeing the final contribution rates. Some employers may accept their proposed contribution rates quite readily whilst others may want to explore their options. You may want us to look at the viability of **different contribution strategies** that are proposed by individual employers.
- Once a set of final contribution rates have been agreed for all employers, we will provide you with a **final valuation report** which will clearly set out the final valuation results and will meet all the relevant regulatory requirements. Included in this report will be the Certificate of Rates and Adjustments, which will certify the minimum contribution rates to be paid by each employer for the three year period beginning on 1 April 2017. This final valuation report must be provided to you no later than 31 March 2017.

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## Appendix – Reliances and limitations

This document has been requested by and is provided to Hertfordshire County Council in its capacity as Administering Authority to the Hertfordshire County Council Pension Fund. It has been prepared by Hymans Robertson LLP to support a discussion on funding strategy with the Fund as part of the 2016 funding valuation.

This document should not be released or otherwise disclosed to any third party (including Fund employers) without our prior written consent, in which case it should be released in its entirety. Hymans Robertson LLP accepts no liability to any other party unless we have expressly accepted such liability

### Reliances and limitations

This document has been prepared for the purpose of communicating the initial results of the 2016 valuation at whole fund level. Nothing contained within it affects any member's benefits. Furthermore, none of the figures should be used for accounting purposes (e.g. under FRS102 or IAS19) or for any other purpose (e.g. a termination valuation).

The valuation results are wholly dependent on the data provided to us and the assumptions that we use in our calculations. We have previously issued a separate report confirming that the data provided is fit for the purposes of this valuation and have commented on our perception of the quality of the data provided. The data used in our calculations will be set out in our data report to follow.

It is possible that as part of our ongoing discussions you may find that there is additional information you should provide us with. In a similar way, you may feel that one or more of the assumptions is no longer not suitable for the Fund

and you may wish to explore the use of alternatives. Until both of these areas are definitively agreed by all relevant parties, the results in this document will remain "initial" and could be subject to change before the final valuation report is signed off.

This document is a "component report" of the eventual final aggregate valuation report due to be completed by 31 March 2017.

The results contained in this document are for the Fund as a whole. It does not set out the valuation results for individual employers, which will be derived at a later date. Employers come in different shapes and sizes and their valuation results are not uniform. We would advise against extrapolating the results contained in this document to predict possible contribution rates for employers at this stage.

The figures in this report are based on our understanding of the benefit structure of the LGPS as at 31 March 2016.

### Actuarial Standards

The following Technical Actuarial Standards<sup>1</sup> are applicable in relation to this report and have been complied with where material:

- TAS R – Reporting;
- TAS D – Data;
- TAS M – Modelling; and
- Pensions TAS.

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<sup>1</sup> Technical Actuarial Standards (TASs) are issued by the Financial Reporting Council (FRC) and set standards for certain items of actuarial work.

# FUNDING STRATEGY STATEMENT

November 2016

Hertfordshire Pension Fund  
Local Government Pension Scheme



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# 1 Introduction

## 1.1 What is this document?

This is the Funding Strategy Statement (FSS) of the Hertfordshire Pension Fund (“the Fund”), which is administered by Hertfordshire County 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. It is effective from 31 March 2017.

## 1.2 What is the Hertfordshire Pension Fund?

The Fund is part of the national Local Government Pension Scheme (LGPS). The LGPS was set up by the UK Government to provide retirement and death benefits for local government employees, and those employed in similar or related bodies, across the whole of the UK. The Administering Authority runs the Hertfordshire Fund, in effect the LGPS for the Hertfordshire area, to make sure it:

- receives the proper amount of contributions from employees and employers, and any transfer payments;
- invests the contributions appropriately, with the aim that the Fund’s assets grow over time with investment income and capital growth; and
- uses the assets to pay Fund benefits to the members (as and when they retire, for the rest of their lives), and to their dependants (as and when members die), as defined in the LGPS Regulations. Assets are also used to pay transfer values and administration costs.

The roles and responsibilities of the key parties involved in the management of the Fund are summarised in [Appendix A](#).

## 1.3 Why does the Fund need a Funding Strategy Statement?

Employees’ benefits are guaranteed by the LGPS Regulations, and do not change with market values or employer contributions. Investment returns will help pay for some of the benefits, but probably not all, and certainly with no guarantee. Employees’ contributions are fixed in those Regulations also, at a level which covers only part of the cost of the benefits.

Therefore, employers need to pay the balance of the cost of delivering the benefits to members and their dependants.

The FSS focuses on how employer liabilities are measured, the pace at which these liabilities are funded, and how employers or pools of employers pay for their own liabilities. This statement sets out how the Administering Authority has balanced the conflicting aims of:

- affordability of employer contributions,
- transparency of processes,
- stability of employers’ contributions, and
- prudence in the funding basis.

The requirement to maintain and publish an FSS is also contained in the LGPS Regulations, as set out in [Appendix B](#).

The FSS is a summary of the Fund's approach to funding its liabilities and when other funding decisions are required, for example when employers join or leave the Fund. It is not an exhaustive statement of policy on all issues. The FSS forms part of a framework which includes:

- the LGPS Regulations;
- the Rates and Adjustments Certificate (confirming employer contribution rates for the next three years) which can be found in an appendix to the formal valuation report;
- the Fund's policies on admissions and cessations;
- actuarial factors for valuing individual transfers, early retirement costs and the costs of buying added service; and
- the Fund's Investment Strategy Statement (see [section 4](#) Funding strategy and links to investment strategy)

Further details on the Pension Fund's policies and strategies can be found on the Pension Fund's website at:

<http://www.yourpension.org.uk/Hertfordshire/Fund-information/Policy-statements.aspx>

#### **1.4 How does the Fund and this FSS affect me?**

This depends on who you are:

- a member of the Fund, i.e. a current or former employee, or a dependant: the Fund needs to be sure it is collecting and holding enough money so that your benefits are always paid in full;
- an employer in the Fund (or which is considering joining the Fund): you will want to know how your contributions are calculated, that these are fair by comparison to other employers in the Fund, and in what circumstances you might need to pay more. Note that the FSS applies to all employers participating in the Fund;
- an Elected Member whose council participates in the Fund: you will want to be sure that the council balances the need to hold prudent reserves for members' retirement and death benefits, with the other competing demands for council money;
- a Council Tax payer: your council seeks to strike the balance above, and also to minimise cross-subsidies between different generations of taxpayers.

#### **1.5 What does the FSS aim to do?**

The FSS sets out the objectives of the Fund's funding strategy, including:

- to ensure the long-term solvency of the Fund, using a prudent long term view. This will ensure that sufficient funds are available to meet all members'/dependants' benefits as they fall due for payment;
- to ensure that employer contribution rates are reasonably stable where appropriate;
- to minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return;
- to reflect the different characteristics of different employers in determining contribution rates. This involves the Fund having a clear and transparent funding strategy to demonstrate how each employer can best meet its own liabilities over future years; and

- 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.

## 1.6 How do I find my way around this document?

In [Section 2](#) there is a brief introduction to some of the main principles behind funding, i.e. deciding how much an employer should contribute to the Fund from time to time.

In [Section 3](#) we outline how the Fund calculates the contributions payable by different employers in different situations.

In [Section 4](#) we show how the funding strategy is linked with the Fund's investment strategy.

In the Appendices we cover various issues in more detail:

- A. The responsibilities of key parties
- B. The regulatory framework, including how and when the FSS is reviewed,
- C. The calculation of employer contributions
- D. The Actuarial assumptions which the Fund Actuary currently makes about the future,
- E. Key risks and controls for the Fund ,
- F. Glossary

If you have any other queries please contact the Pensions Team at [Pensions.Team@hertfordshire.gov.uk](mailto:Pensions.Team@hertfordshire.gov.uk).



## 2 Basic Funding issues

### 2.1 How does the actuary measure the required contribution rate?

In essence this is a three-step process:

1. Calculate the ultimate funding target for that employer, i.e. the ideal amount of assets it should hold in order to be able to pay all its members' benefits. See Appendix C for more details of what assumptions we make to determine that funding target;
2. Determine the time horizon over which the employer should aim to achieve that funding target. See the table in section [3.3](#) and [Note \(c\)](#) for more details;
3. Calculate the employer contribution rate such that it has at least a given probability of achieving that funding target over that time horizon, allowing for different likelihoods of various possible economic outcomes over that time horizon. See 2.4 below and the table in 3.3 [Note \(e\)](#) for more details.

### 2.2 What is each employer's contribution rate?

This is described in more detail in Appendix D. Employer contributions are normally made up of two elements:

- a) the estimated cost of benefits being built up each year, after deducting the members' own contributions and including administration expenses. This is referred to as the "*Primary rate*", and is expressed as a percentage of members' pensionable pay; plus
- b) an adjustment for the difference between the Primary rate above, and the actual contribution the employer needs to pay, referred to as the "*Secondary rate*". In broad terms, if the employer has a pensions deficit, payment of the Secondary rate will aim to return the employer to full funding over an appropriate period (the "time horizon"). The Secondary rate may be expressed as a percentage of pay and/or a monetary amount in each year.

The rates for all employers are shown in the Fund's Rates and Adjustments Certificate, which forms part of the formal Actuarial Valuation Report (<http://www.yourpension.org.uk/Hertfordshire/Fund-information/Policy-statements.aspx>). Employers' contributions are expressed as minima, with employers able to pay contributions at a higher rate. Any additional contributions over and above the certified rate will be considered by the Fund actuary at subsequent valuations, i.e. will be reflected as a credit when next calculating the employer's contributions.

### 2.3 What different types of employer participate in the Fund?

Historically the LGPS was intended for local authority employees only. However over the years, with the diversification and changes to delivery of local services, many more types and numbers of employers now participate. There are currently more employers in the Fund than ever before, largely a result of schools transferring to academy status and services being outsourced from scheme employers such as Councils.

In essence, participation in the LGPS is open to public sector employers providing some form of service to the local community. Whilst the majority of members will be local authority employees (and ex-employees), the majority of participating employers are those providing services in place of (or alongside) local authority services.

The LGPS Regulations define various types of employer as follows:

- **Scheduled bodies** - councils, and other specified employers such as academies and further education establishments. These must provide access to the LGPS in respect of their employees who are not eligible to join another public sector scheme (such as the Teachers Pension Scheme). These employers are so-called because they are specified in a schedule to the LGPS Regulations.

It is now possible for Local Education Authority schools to convert to academy status, and for other forms of school (such as Free Schools) to be established under the academies legislation. All such academies (or Multi Academy Trusts), as employers of non-teaching staff, become separate new employers in the Fund. As academies are defined in the LGPS Regulations as “Scheduled Bodies”, the Administering Authority has no discretion over whether to admit them to the Fund, and the academy has no discretion whether to continue to allow its non-teaching staff to join the Fund. There has also been guidance issued by the DCLG regarding the terms of academies’ membership in LGPS Funds.

- **Designating employers** - employers such as town and parish councils are able to participate in the LGPS via a resolution (and the Fund cannot refuse them entry where the resolution is passed). These employers can designate which of their employees are eligible to join the scheme.
- Other employers are able to participate in the Fund via an admission agreement, and are referred to as ‘**admission bodies**’. These employers are generally those with a “community of interest” with another scheme employer – **community admission bodies** (“CAB”) or those providing a service on behalf of a scheme employer – **transferee admission bodies** (“TAB”). CABs will include housing associations and charities, TABs will generally be contractors. The Fund is able to set its criteria for participation by these employers and can refuse entry if the requirements as set out in the Fund’s admissions policy are not met. The terminology CAB and TAB has been dropped from recent LGPS Regulations, which instead combine both under the single term ‘admission bodies’; however, we have retained the old terminology as we consider it to be helpful in setting funding strategies for these different employers.

## 2.4 How does the contribution rate vary for different employers?

All three steps outlined in section 2.1 are considered when setting contributions (more details are given in [Section 3](#) and [Appendix D](#)).

1. The **funding target** is based on a set of assumptions about the future, (e.g. investment returns, inflation, pensioners’ life expectancies). An employer’s individual funding target is set so that there are sufficient assets to pay for all accrued benefits at the end of its participation in the Fund and that the employers liabilities do not fall on other employers in the Fund in the future;
2. The **time horizon** required is, in broad terms, the period over which any deficit is to be recovered. A shorter period will lead to higher contributions, and vice versa (all other things being equal). Employers may be given a lower time horizon if they have a less permanent anticipated membership, or do not have tax-raising powers to increase contributions if investment returns under-perform; and
3. The **probability of achieving** the funding target over that time horizon will be dependent on the Fund’s view of the strength of employer covenant and its funding profile. Where an employer is considered to be weaker, or potentially ceasing from the Fund, then the required probability will be set higher, which in turn will increase the required contributions (and vice versa).

## 2.5 How is a deficit (or surplus) calculated?

An employer's "funding level" is defined as the ratio of:

- the market value of the employer's share of assets (see Appendix D, section D5, for further details of how this is calculated), to;
- the value placed by the actuary on the benefits built up to date for the employer's employees and ex-employees (the "liabilities"). The Fund actuary agrees with the Administering Authority the assumptions to be used in calculating this value.

If this ratio is less than 100% then it means the employer has a shortfall, which is the employer's deficit; if it is more than 100% then the employer is said to be in surplus. The amount of deficit or shortfall is the difference between the asset value and the liabilities value.

It is important to note that the deficit/surplus and funding level are only measurements at a particular point in time, on a particular set of assumptions about the future. Whilst we recognise that various parties will take an interest in these measures, for most employers the key issue is how likely it is that their contributions will be sufficient to pay for their members' benefits (when added to their existing asset share and anticipated investment returns).

In short, deficits and funding levels are short term measures, whereas contribution-setting is a longer term issue.

## 2.6 How does the Fund recognise that contribution levels can affect council and employer service provision, and council tax?

The Administering Authority and the Fund actuary are acutely aware that, all other things being equal, a higher contribution required to be paid to the Fund will mean less cash available for the employer to spend on the provision of services. However, this is balanced against the following considerations:

- The Fund provides invaluable financial security to local families, whether to those who formerly worked in the service of the local community who have now retired, or to their families after their death;
- The Fund must have the assets available to meet these retirement and death benefits, which in turn means that the various employers must each pay their own way. Lower contributions today will mean higher contributions tomorrow: deferring payments does not alter the employer's ultimate obligation to the Fund in respect of its current and former employees;
- Each employer will generally only pay for its own employees and ex-employees (and their dependants), not for those of other employers in the Fund;
- The Fund strives to maintain reasonably stable employer contribution rates where appropriate and possible. However, a recent shift in regulatory focus means that solvency within each generation is considered by the Government to be a higher priority than stability of contribution rates;
- The Fund wishes to avoid the situation where an employer falls so far behind in managing its funding shortfall that its deficit becomes unmanageable in practice: such a situation may lead to employer insolvency and the resulting deficit falling on the other Fund employers. In that situation, those employers' services would in turn suffer as a result;
- Council contributions to the Fund should be at a suitable level, to protect the interests of different generations of council tax payers. For instance, underpayment of contributions for some years will need to be balanced by overpayment in other years; the council will wish to minimise the extent to which

council tax payers in one period are, in effect, benefitting at the expense of those paying in a different period.

Therefore, there is clearly a balance to be struck between the Fund's need for maintaining prudent funding levels, and the employers' need to allocate their resources appropriately. The Fund achieves this through various techniques which affect contribution increases to various degrees, as discussed in section 3. In deciding which of these techniques to apply to any given employer, the Fund will consider a risk assessment of that employer using a knowledge base which is regularly monitored and kept up-to-date. This database will include such information as the type of employer, its membership profile and funding position, any guarantors or security provision, material changes anticipated, etc. This helps the Fund establish a picture of the financial standing of the employer, i.e. its ability to meet its long term Fund commitments. To ensure that the information is kept up to date, employers are required to complete an annual survey to confirm the accuracy of information held on the database.

Where an employer is considered relatively low risk then the Fund will permit options such as stabilisation (see 3.3 [Note \(b\)](#)), a longer time horizon relative to other employers, and/or a lower probability of achieving their funding target. Such options will temporarily produce lower contribution levels than would otherwise have applied. This is permitted in the expectation that the employer will still be able to meet its obligations for many years to come.

An employer whose risk assessment indicates a less strong covenant i.e their assessed financial strength in regards to their ability to pay for pension obligations in the long run, will generally be required to pay higher contributions (for instance, with a higher funding target, and/or a shorter deficit recovery period relative to other employers, and/or a higher probability of achieving the target). This is because of the higher probability that at some point it will fail or be unable to meet its pension contributions, with its deficit in the Fund then falling to other Fund employers, or because the employer has less time to meet its obligations to the Fund.

## 3 Calculating contributions for individual Employers

### 3.1 General comments

A key challenge for the Administering Authority is to balance the need for stable, affordable employer contributions with the requirement to take a prudent, longer-term view of funding and ensure the solvency of the Fund. With this in mind, the Fund's three-step process identifies the key issues:

1. What is a suitably (but not overly) prudent funding target?
2. How long should the employer be permitted to reach that target? This should be realistic but not so long that the funding target is in danger of never actually being achieved.
3. What probability is required to reach that funding target? This will always be less than 100% as we cannot be certain of future market movements. Higher probability "bars" can be used for employers where the Fund wishes to reduce the risk that the employer ceases leaving a deficit to be picked up by other employers.

These and associated issues are covered in this Section.

The Administering Authority recognises that there may occasionally be particular circumstances affecting individual employers that are not easily managed within the rules and policies set out in the Funding Strategy Statement. Therefore the Administering Authority may, at its sole discretion, direct the actuary to adopt alternative funding approaches on a case by case basis for specific employers.

### 3.2 The effect of paying contributions below the measured level

There are a number of methods which the Administering Authority may permit, in order to improve the stability of employer contributions. These include, where circumstances permit:

- capping of employer contribution rate changes within a pre-determined range ("stabilisation");
- the use of extended time horizons;
- adjusting the required probability of meeting the funding target;
- the phasing in of contribution rises or reductions;
- the pooling of contributions amongst employers with similar characteristics; and/or
- the use of some form of security or guarantee to justify a lower contribution rate than would otherwise be the case.

Employers which are permitted to use one or more of the above methods will often be paying, for a time, contributions less than the measured contribution rate. Such employers should appreciate that:

- their true long term liability (i.e. the actual eventual cost of benefits payable to their employees and ex-employees) is not affected by the choice of method,
- lower contributions in the short term will be assumed to incur a greater loss of investment returns on the deficit. Thus, deferring a certain amount of contribution may lead to higher contributions in the long-term, and
- it may take longer to reach their funding target, all other things being equal.

Section 3.3 summarises how the main funding policies differ for different types of employer, followed by more detailed notes where necessary. Section 3.4 onwards deals with funding issues which apply to all employers.

### 3.3 The different approaches used for different employers

Type of employer	Scheduled Bodies			Designating Employers	Community Admission Bodies		Transferee Admission Bodies	
Sub-type	Local Authorities & Police	Academies	Other scheduled bodies	Parish & Town Councils	Open to new entrants	Closed to new entrants		
<b>Funding Target Basis used</b>	Ongoing, assumes long-term Fund participation (see <a href="#">Appendix C</a> )				Ongoing, but may move to “gilts basis” - see <a href="#">note (a)</a>		Ongoing, assumes fixed contract term in the Fund (see <a href="#">Appendix C</a> )	
<b>Primary rate approach</b>	(see <a href="#">Appendix D, section D.2</a> )							
<b>Stabilised contribution rate?</b>	Yes see <a href="#">note (b)</a>	Yes see <a href="#">note (b)</a>	No	No	No	No	No	
<b>Maximum time horizon see <a href="#">note (c)</a></b>	20 years	20 years	20 years	TBC	Future working lifetime of members	Future working lifetime of members	Outstanding contract term	
<b>Secondary rate see <a href="#">note (d)</a></b>	% of payroll or monetary amount	% of payroll	% of payroll or monetary amount	% of payroll	% of payroll or monetary amount	Monetary amount	% of payroll or monetary amount	
<b>Treatment of surplus</b>	Covered by stabilisation arrangement	Covered by stabilisation arrangement	Preferred approach: contributions kept at future service rate. However, reductions may be permitted by the Admin. Authority				Reduce contributions by spreading the surplus over the remaining contract term	
<b>Probability of achieving target see <a href="#">note (e)</a></b>	66%	66%	TBC	TBC	TBC	TBC	TBC	TBC
<b>Phasing of contribution changes</b>	Covered by stabilisation arrangement	Covered by stabilisation arrangement	Max 3 years	Max 3 years	Max 3 years	Max 3 years	Max 3 years	None
<b>Review of rates see <a href="#">note (f)</a></b>	Administering Authority reserves the right to review contribution rates and amounts, and the level of security provided, at regular intervals between valuations						Particularly reviewed at regular intervals in last 3 years of contract	
<b>New employer</b>	n/a	see <a href="#">note (g)</a>	n/a	See <a href="#">section 2.3</a>	See <a href="#">note (h)</a>		See <a href="#">notes (h) &amp; (i)</a>	
<b>Cessation of participation: cessation debt payable</b>	Cessation is assumed not to be generally possible, as Scheduled Bodies are legally obliged to participate in the LGPS. In the rare event of cessation occurring, the cessation debt principles applied would be as per <a href="#">Note (i)</a> .				Can be ceased subject to terms of admission agreement. Cessation debt will be calculated on a basis appropriate to the circumstances of cessation. See <a href="#">Note (j)</a> .		Participation assumed to expire at the end of the contract. Cessation debt calculated on ongoing basis. Awarding Authority liable for future deficits and contributions arising.	

### Note (a) Basis for CABs closed to new entrants

In the circumstances where:

- the employer is an Admission Body but not a Transferee Admission Body, and
- the employer has no guarantor for future deficits and contributions, and
- the admission agreement is likely to terminate, or the employer is likely to lose its last active member, within a timeframe considered appropriate by the Administering Authority to prompt a change in funding,

the Administering Authority may set a higher funding target (e.g. using a discount rate set equal to gilt yields) by the time the agreement terminates or the last active member leaves, in order to protect other employers in the Fund. This policy will increase regular contributions and reduce, but not entirely eliminate, the possibility of a final deficit payment being required from the employer when a cessation valuation is carried out.

The Administering Authority also reserves the right to adopt the above approach in respect of those Admission Bodies whose admission agreement is open or where there is no immediate expectation that the admission agreement will cease, where there is no guarantor for future deficits and contributions, or where the strength of covenant is considered to be weak.

### Note (b) Stabilisation

Stabilisation is a mechanism where employer contribution rate variations from year to year are kept within a pre-determined range, thus allowing those employers' rates to be relatively stable. In the interests of stability and affordability of employer contributions, the Administering Authority, on the advice of the Fund Actuary, believes that stabilising contributions can still be viewed as a prudent longer-term approach. However, employers whose contribution rates have been "stabilised" (and may therefore be paying less than their theoretical contribution rate) should be aware of the risks of this approach and should consider making additional payments to the Fund if possible.

This stabilisation mechanism allows short term investment market volatility to be managed so as not to cause volatility in employer contribution rates, on the basis that a long term view can be taken on net cash inflow, investment returns and strength of employer covenant.

In general, stabilisation will only be considered for employers who are:

- Scheduled bodies that have tax raising powers, or are part of a pool
- Open to new entrants
- Have a long term time horizon in the Fund
- Have been assessed as having a strong employer covenant so as to protect the Fund and the other employers in the Fund against the risk of the employer defaulting in relation to its liabilities.

The current stabilisation mechanism applies if:

- the employer satisfies the eligibility criteria set by the Administering Authority, as set out above and;
- there are no material events which cause the employer to become ineligible, e.g. significant reductions in active membership (due to outsourcing or redundancies), or changes in the nature of the employer (perhaps due to Government restructuring).

On the basis of extensive modelling carried out for the 2016 valuation exercise (see [Section 4](#)), the stabilisation parameters have been set allowing for increases/decreased of 0% to 1.5% of pay.

The stabilisation criteria and limits will be reviewed at the 31 March 2019 valuation, to take effect from 1 April 2020.

#### **Note (c) Maximum time horizon**

The maximum time horizon starts at the commencement of the revised contribution rate (1 April 2017 for the 2016 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 time horizons, for example where there were no new entrants.

#### **Note (d) Secondary rate**

For employers where stabilisation is not being applied, the Secondary contribution rate for each employer covering the three year period until the next valuation will often 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 relatively mature, i.e. has a large Secondary contribution rate (e.g. above 15% of payroll), 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.

#### **Note (e) Probability of achieving funding target**

Each employer has their funding target calculated, and a relevant time horizon over which to reach that target. Contributions are set such that, combined with the employer's current asset share and anticipated market movements over the time horizon, the funding target is achieved with a given minimum probability. A higher required probability bar will give rise to higher required contributions, and vice versa.

The way in which contributions are set using these three steps, and relevant economic projections, is described in further detail in [Appendix D](#).

Different probabilities are set for different employers depending on their nature and circumstances: in broad terms, a higher probability will apply due to one or more of the following:

- the Fund believes the employer poses a greater funding risk than other employers,
- the employer does not have tax-raising powers;
- the employer does not have a guarantor or other sufficient security backing its funding position; and/or
- the employer is likely to cease participation in the Fund in the short or medium term.

#### **Note (f) Regular Reviews**

The Fund reserves the right to review contribution rates and amounts, and the level of security provided, at regular intervals between Valuations. Such reviews may be triggered by significant events including but not limited to: 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 (by strengthening the actuarial assumptions adopted and/or moving to monetary levels of deficit recovery contributions), and/or an increased level of security or guarantee.

#### **Note (g) New Academy conversions**

At the time of writing, the Fund's policies on academies' funding issues are as follows:

- i. The new academy will be regarded as a separate employer in the scheme in its own right.
- ii. The new academy's past service liabilities on conversion will be calculated based on its active Fund members on the day before conversion. For the avoidance of doubt, these liabilities will include all past service of those members, but will exclude the liabilities relating to any ex-employees of the school who have deferred or pensioner status;
- iii. The new academy will be allocated an initial asset share from the ceding council's assets in the Fund. This asset share will be calculated using the estimated funding position of the ceding council at the date of academy conversion. The share will be based on the active members' funding level, having first allocated assets in the council's share to fully fund deferred and pensioner members. The asset allocation will be based on market conditions and the academy's active Fund membership on the day prior to conversion;
- iv. Schools that convert to Academy status who are already in the Schools & Academies Pool will continue to pay the prevailing rate of the pool until the next Triennial Valuation, at which they have the opportunity to opt out if they wish to have an individual employer contribution rate calculated;

The Fund's policies on academies are subject to change in the light of any amendments to DCLG guidance. Any changes will be notified to academies, and will be reflected in a subsequent version of this FSS. In particular, policies (iv) and (v) above will be reconsidered at each valuation.

#### **Note (h) New Admission Bodies**

With effect from 1 October 2012, the LGPS 2012 Miscellaneous Regulations introduced mandatory new requirements for all Admission Bodies brought into the Fund from that date. Under these Regulations, all new Admission Bodies will be required to provide some form of security, such as a guarantee from the letting employer, an indemnity, or a bond. The security is required to cover some or all of the following:

- the strain cost of any redundancy early retirements resulting from the premature termination of the contract;
- allowance for the risk of asset underperformance;
- allowance for the risk of a fall in gilt yields;
- allowance for the possible non-payment of employer and member contributions to the Fund; and/or
- the current deficit.

Any security must be to the satisfaction of the Administering Authority and where applicable to the letting employer, and will be reassessed at regular intervals. See also [Note \(i\)](#) below

The Fund will only consider requests from "CAB's" or other similar bodies to join the Fund if they are sponsored by a scheduled body with tax raising powers who will guarantee the liabilities of the body and supplemented, where appropriate, by the provision of a form of security as above.

The above approaches reduce the risk, to other employers in the Fund, of potentially having to pick up any shortfall in respect of Admission Bodies ceasing with an unpaid deficit.

#### **Note (i) New Transferee Admission Bodies**

A new TAB usually joins the Fund as a result of the letting/outsourcing of some services from an existing employer (normally a Scheduled Body such as a council or academy) to another organisation (a “contractor”). This involves the TUPE transfer of some staff from the letting employer to the contractor. Consequently, for the duration of the contract, the contractor can seek admitted body status in the Fund so that the transferring employees maintain their eligibility for LGPS membership. At the end of the contract the employees revert to the letting employer or to a replacement contractor.

Ordinarily, the TAB would be set up in the Fund as a new employer with responsibility for all the accrued benefits of the transferring employees; in this case, the contractor would usually be assigned an initial asset allocation equal to the past service liability value of the employees’ Fund benefits. The quid pro quo is that the contractor is then expected to ensure that its share of the Fund is also fully funded at the end of the contract: see Note (j).

Employers who “outsource” have flexibility in the way that they can deal with the pension risk potentially taken on by the contractor. In particular there are three different routes that such employers may wish to adopt. Clearly as the risk ultimately resides with the employer letting the contract, it is for them to agree the appropriate route with the contractor:

- Pooling: Under this option the contractor is pooled with the letting employer. In this case, the contractor pays the same rate as the letting employer, which may be under a stabilisation approach.
- Letting employer retains pre-contract risks: Under this option the letting employer would retain responsibility for assets and liabilities in respect of service accrued prior to the contract commencement date. The contractor would be responsible for the future liabilities that accrue in respect of transferred staff. The contractor’s contribution rate could vary from one valuation to the next. It would be liable for any deficit at the end of the contract term in respect of assets and liabilities attributable to service accrued during the contract term.
- Fixed contribution rate agreed: Under this option the contractor pays a fixed contribution rate and does not pay any cessation deficit. Any surplus or deficit present at the end of the contract period falls back to the letting employer.

The Administering Authority is willing to administer any of the above options as long as the approach is documented in the Admission Agreement as well as the transfer agreement. The Admission Agreement should ensure that some element of risk transfers to the contractor where it relates to their decisions and it is unfair to burden the letting employer with that risk. For example the contractor should typically be responsible for pension costs that arise from:

- above average pay increases, including the effect in respect of service prior to contract commencement even if the letting employer takes on responsibility for the latter under (ii) above; and
- redundancy and early retirement decisions.

#### **Note (j) Admission Bodies Ceasing**

Notwithstanding the provisions of the Admission Agreement, the Administering Authority may consider any of the following as triggers for the cessation of an admission agreement with any type of body:

- Last active member ceasing participation in the Fund (NB recent LGPS Regulation changes mean that the Administering Authority has the discretion to defer taking action for up to three years, so that if the employer acquires one or more active Fund members during that period then cessation is not triggered. However, this may or may not be applied in any given case);
- 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 an appropriate alternative guarantor, as required by the Fund.

In the case of a transferee admission body, participation is assumed to expire at the end of the contract.

On cessation, the Administering Authority will instruct the Fund actuary to carry out a cessation valuation to determine whether there is any deficit or surplus. Where there is a deficit, payment of this amount in full would normally be sought from the Admission Body; where there is a surplus it should be noted that under current legislation there is no mechanism to refund payment to the Admission Body.

For transferee admission bodies, the cessation valuation will normally be calculated using the ongoing basis, in line with the basis on which they were admitted to the Fund. The original letting/outsourcing employer will then be liable for future deficits and contributions arising.

For non-Transferee Admission Bodies whose participation is voluntarily ended either by themselves or the Fund, or where a cessation event has been triggered, the Administering Authority must look to protect the interests of other ongoing employers. The actuary will therefore adopt an approach which, to the extent reasonably practicable, protects the other employers from the likelihood of any material loss emerging in future:

- a) Where there is a guarantor for future deficits and contributions, the cessation valuation will normally be calculated using the ongoing basis as described in Appendix C;
- b) Alternatively, it may be possible to simply transfer the former Admission Body's liabilities and assets to the guarantor, without needing to crystallise any deficit. This approach may be adopted where the employer cannot pay the contributions due, and this is within the terms of the guarantee;
- c) Where a guarantor does not exist for future deficits and contributions then, in order to protect other employers in the Fund, the cessation liabilities and final deficit will normally be calculated using a "gilts cessation basis", which is more prudent than the ongoing basis. This has no allowance for potential future investment outperformance above gilt yields, and has added allowance for future improvements in life expectancy. This could give rise to significant cessation debts being required.

Any shortfall would usually be levied on the departing Admission Body as a single lump sum payment. If this is not possible then the Fund would look to any bond, indemnity or guarantee in place for the employer.

In the event that the Fund is not able to recover the required payment in full, then the unpaid amounts fall to be shared amongst all of the other employers in the Fund. This may require an immediate revision to the Rates and Adjustments Certificate affecting other employers in the Fund, or instead be reflected in the contribution rates set at the next formal valuation following the cessation date.

As an alternative, 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. Under this

agreement the Fund would accept an appropriate alternative security to be held against any deficit, and would carry out the cessation valuation on an ongoing basis: deficit recovery payments would be derived from this cessation debt. This approach would be monitored as part of each triennial valuation: the Fund reserves the right to revert to a “gilts cessation basis” and seek immediate payment of any funding shortfall identified. The Administering Authority may need to seek legal advice in such cases, as the Body would have no contributing members.

### 3.4 Pooled contributions

From time to time, with the advice of the Actuary, the Administering Authority may set up pools for employers with similar or complementary characteristics. This will always be in line with its broader funding strategy. The exceptions are Transferee admission bodies and community admission bodies that are deemed by the Administering Authority to have closed to new entrants. The current pools in place within the Fund are as follows:

- Hertfordshire maintained schools, academies, free schools, university technical colleges and studio schools; and
- Parish and Town Councils

Those employers which have been pooled are identified in the Rates and Adjustments Certificate.

Employers who participate in a pool, will be required to comply with the conditions and requirements set out in the pooling policy applicable to that Pool, which can be found at:

<http://www.yourpension.org.uk/Hertfordshire/Fund-information/Policy-statements.aspx>.

Employers will be advised of their individual funding positions as well as that of the pool at each Valuation. In paying a pooled contribution rate, Pool Members must acknowledge that they may be paying a rate that is more or less than the employer contribution rate that would have been payable if the employer contribution rate had been determined on an individual employer basis. Pool Members may wish to consider making additional payments to the Pension Fund to improve their funding/balance sheet position, particularly where their funding level is lower than that of the rest of the pool.

### 3.5 Additional flexibility in return for added security

At its discretion, the Administering Authority may permit greater flexibility to the employer’s contributions if the employer provides added security to the satisfaction of the Administering Authority.

Such flexibility includes a reduced rate of contribution, an extended time horizon, or permission to join a pool with another body (e.g. the Local Authority).

Such security may include, but is not limited to, a suitable bond, a legally-binding guarantee from an appropriate third party, or security over an employer asset of sufficient value.

The degree of flexibility given may take into account factors such as:

- the extent of the employer’s deficit;
- the amount and quality of the security offered;
- the employer’s financial security and business plan; and
- whether the admission agreement is likely to be open or closed to new entrants.

### 3.6 Non ill health early retirement costs

It is assumed that members' benefits 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). Note the relevant age may be different for different periods of service, following the benefit changes from April 2008 and April 2014. Employers are required to pay additional contributions ('strain') wherever an employee retires before attaining this age. Strain costs are payable in full in the year of retirement. The actuary's funding basis makes no allowance for premature retirement except on grounds of ill-health.

### 3.7 Ill health early retirement costs

In the event of a member's early retirement on the grounds of ill-health, a funding strain will usually arise, which can be very large. Such strains are currently met by each employer, although individual employers may elect to take external insurance (see 3.8 below).

Employers will usually have an 'ill health allowance' as calculated at each Valuation. The Fund monitors each employer's ill health experience on an ongoing basis. If the cumulative cost 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 apply for non ill-health cases, as outlined in the Fund's Administration Strategy and in the case of admission bodies, in each separate Admission Agreement.

### 3.8 External Ill health insurance

If an employer provides satisfactory evidence to the Administering Authority of a current external insurance policy covering ill health early retirement strains, then:

- 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, and
- there is no need for monitoring of allowances.

The employer must keep the Administering Authority notified of any changes in the insurance policy's coverage or premium terms, or if the policy is ceased.

### 3.9 Employers with no remaining active members

In general an employer ceasing in the Fund, due to the departure of the last active member, will pay a cessation debt on an appropriate basis (see 3.3, Note (j)) and consequently have no further obligation to the Fund.

Thereafter it is expected that one of two situations will eventually arise:

- a) The employer's asset share runs out before all its ex-employees' benefits have been paid. In this situation the other Fund employers will be required to contribute to pay all remaining benefits: this will be done by the Fund actuary apportioning the remaining liabilities on a pro-rata basis at successive formal valuations;
- b) The last ex-employee or dependant dies before the employer's asset share has been fully utilised. In this situation the remaining assets would be apportioned pro-rata by the Fund's actuary to the other Fund.

In exceptional circumstances the Fund may permit an employer with no remaining active members to continue contributing to the Fund. This would require the provision of a suitable security or guarantee, as well as a written ongoing commitment to fund the remainder of the employer's obligations over an appropriate period. The Fund would reserve the right to invoke the cessation requirements in the future, however. The Administering Authority may need to seek legal advice in such cases, as the employer would have no contributing members.

### 3.10 Policies on bulk transfers

The Fund will consider bulk transfers on a case by case basis, but in general:

- The Fund will not pay bulk transfers greater than the lesser of (a) the asset share of the transferring employer in the Fund, and (b) the value of the past service liabilities of the transferring members;
- The Fund will not grant added benefits to members bringing in entitlements from another Fund unless the asset transfer is sufficient to meet the added liabilities; and
- The Fund may permit shortfalls to arise on bulk transfers if the Fund employer has suitable strength of covenant and commits to meeting that shortfall in an appropriate period. This may require the employer's Fund contributions to increase between valuations.

## 4 Funding strategy and links to investment strategy

### 4.1 What is the Fund's investment strategy?

The Fund has built up assets over the years, and continues to receive contributions and other income. All of this must be invested in a suitable manner, which is the investment strategy.

The Investment strategy is set by the administering authority, and after taking investment advice. The precise mix, manager make up and target returns are set out in the Investment Strategy Statement, which is accessible from the Fund's website: <http://www.yourpension.org.uk/Hertfordshire/Fund-information/Policy-statements.aspx>

The investment strategy is set for the long-term, but is reviewed from time to time. Normally a full review is carried out as part of each actuarial valuation, and is kept under review annually between actuarial valuations to ensure that it remains appropriate to the Fund's liability profile.

The same investment strategy is currently followed for all employers.

### 4.2 What is the link between funding strategy and investment strategy?

The Fund must be able to meet all benefit payments as and when they fall due. These payments will be met by contributions (resulting from the funding strategy) or asset returns and income (resulting from the investment strategy). To the extent that investment returns or income fall short, then higher cash contributions are required from employers, and vice versa

Therefore, the funding and investment strategies are inextricably linked.

### 4.3 How does the funding strategy reflect the Fund's investment strategy?

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 contained in the discount rate (see Appendix C3) is within a range that would be considered acceptable for funding purposes; it is also considered to be consistent with the requirement to take a "prudent longer-term view" of the funding of liabilities as required by the UK Government (see Appendix B1).

However, in the short term – such as the three yearly assessments at formal valuations – there is the scope for considerable volatility and there is a material chance that in the short-term and even medium term, asset returns will fall short of this target. The stability measures described in [Section 3](#) 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.

### 4.4 How does this differ for a large stable employer?

The Actuary has developed four key measures which capture the essence of the Fund's strategies, both funding and investment:

- Prudence - the Fund should have a reasonable expectation of being fully funded in the long term;
- Affordability – how much can employers afford;
- Stewardship – the assumptions used should be sustainable in the long term, without having to resort to overly optimistic assumptions about the future to maintain an apparently healthy funding position; and
- Stability – employers should not see significant moves in their contribution rates from one year to the next, to help provide a more stable budgeting environment.

The problem is that the key objectives often conflict. For example, minimising the long term cost of the scheme (i.e. keeping employer rates affordable) is best achieved by investing in higher returning assets e.g. equities. However, equities are also very volatile (i.e. go up and down fairly frequently in fairly large moves), which conflicts with the objective to have stable contribution rates.

Therefore, a balance needs to be maintained between risk and reward, which has been considered by the use of Asset Liability Modelling: this is a set of calculation techniques applied by the Fund's actuary to model the range of potential future solvency levels and contribution rates.

The Actuary was able to model the impact of these four key areas, for the purpose of setting a stabilisation approach (see 3.3 Note (b)). The modelling demonstrated that retaining the present investment strategy, coupled with constraining employer contribution rate changes as described in 3.3 Note (b), struck an appropriate balance between the above objectives. In particular the stabilisation approach currently adopted meets the need for stability of contributions without jeopardising the Administering Authority's aims of prudent stewardship of the Fund.

Whilst the current stabilisation mechanism is to remain in place until 2020 and will be reviewed as part of the 2019 valuation.

#### **4.5 Does the Fund monitor its overall funding position?**

The Administering Authority monitors the relative funding position, i.e. changes in the relationship between asset values and the liabilities value, on a quarterly basis and reports this to Pensions Committee and to the LGPS Board.



## 5 Statutory reporting and comparison to other LGPS Funds

### 5.1 Purpose

Under Section 13(4)(c) of the Public Service Pensions Act 2013 (“Section 13”), the Government Actuary’s Department must, following each triennial actuarial valuation, report to the Department of Communities & Local Government (DCLG) on each of the LGPS Funds in England & Wales. This report will cover whether the rate of employer contributions for each fund are set at an appropriate level to ensure both the solvency and the long term cost efficiency of the Fund.

This additional DCLG oversight may have an impact on the strategy for setting contribution rates at future valuations.

### 5.2 Solvency

For the purposes of Section 13, the rate of employer contributions shall be deemed to have been set at an appropriate level to ensure solvency if:

- a) the rate of employer contributions is set to target a funding level for the Fund of 100%, over an appropriate time period and using appropriate actuarial assumptions (where appropriateness is considered in both absolute and relative terms in comparison with other funds); and either
- b) employers collectively have the financial capacity to increase employer contributions, and/or the Fund is able to realise contingent assets should future circumstances require, in order to continue to target a funding level of 100%; or
- c) there is an appropriate plan in place should there be, or if there is expected in future to be, a material reduction in the capacity of fund employers to increase contributions as might be needed.

### 5.3 Long Term Cost Efficiency

The rate of employer contributions shall be deemed to have been set at an appropriate level to ensure long term cost efficiency if:

- a) the rate of employer contributions is sufficient to make provision for the cost of current benefit accrual,
- b) with an appropriate adjustment to that rate for any surplus or deficit in the Fund.

In assessing whether the above condition is met, DCLG may have regard to various absolute and relative measures. DCLG may assess and compare these metrics on a suitable standardised market-related basis, for example where the local funds’ actuarial bases do not make comparisons straightforward.

Relative measures are primarily concerned with comparing the Fund with other LGPS Funds and include:

- the implied deficit recovery period (the estimated period until the Fund reaches a 100% funding level); and
- the investment return required to achieve full funding after 20 years.

Absolute measures are primarily concerned with comparing the Fund with a given objective benchmark and include:

- the extent to which the contributions payable are sufficient to cover the cost of current benefit accrual and the interest cost on any deficit;
- how the required investment return under “relative considerations” above compares to the estimated future return being targeted by the Fund’s current investment strategy;
- the extent to which contributions actually paid have been in line with the expected contributions based on the extant rates and adjustment certificate; and
- the extent to which any new deficit recovery plan can be directly reconciled with, and can be demonstrated to be a continuation of, any previous deficit recovery plan, after allowing for actual Fund experience.

## Appendix A – Responsibilities of key parties

The efficient and effective operation of the Fund needs various parties to each play their part.

### A1 The Administering Authority should:-

1. Operate the Fund in accordance with the LGPS Regulations;
2. Effectively manage any potential conflicts of interest arising from its dual role as Administering Authority and a Fund employer;
3. Collect employer and employee contributions, and investment income and other amounts due to the Fund;
4. Ensure that cash is available to meet benefit payments as and when they fall due;
5. Pay from the Fund the relevant benefits and entitlements that are due;
6. Invest surplus monies (i.e. contributions and other income which are not immediately needed to pay benefits) in accordance with the Fund's Investment Strategy Statement (ISS) and LGPS Regulations;
7. Communicate appropriately with employers so that they fully understand their obligations to the Fund;
8. Take appropriate measures to safeguard the Fund against the consequences of employer default;
9. Manage the valuation process in consultation with the Fund's actuary;
10. Provide data and information as required by the Government Actuary's Department to carry out their statutory obligations (see [Section 5](#));
11. Prepare and maintain a FSS and an ISS, after consultation;
12. Notify the Fund's actuary of material changes which could affect funding (this is covered in a separate agreement with the actuary); and
13. Monitor all aspects of the fund's performance and funding and amend the ISS as necessary and appropriate.

### A2 The Individual Employer should:-

1. Deduct contributions from employees' pay correctly;
2. Pay all contributions, including their own as determined by the actuary, promptly by the due date;
3. Establish and exercise a discretions policy within the regulatory framework;
4. Make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of scheme benefits, early retirement strain; and
5. Notify the Administering Authority promptly of all changes to its circumstances, prospects or membership, which could affect future funding.
6. In the case of admission bodies, ensure completion of admission agreements prior to contract commencement.

**A3 The Fund Actuary should:-**

1. Prepare valuations, including the setting of employers' contribution rates. This will involve agreeing assumptions with the Administering Authority, having regard to the FSS and LGPS Regulations, and targeting each employer's solvency appropriately;
2. Provide data and information as required by the Government Actuary's Department to carry out their statutory obligations (see [Section 5](#));
3. Provide advice relating to new employers in the Fund, including the level and type of bonds or other forms of security (and the monitoring of these);
4. Prepare advice and calculations in connection with bulk transfers and individual benefit-related matters;
5. Assist the Administering Authority in considering possible changes to employer contributions between formal valuations, where circumstances suggest this may be necessary;
6. Advise on the termination of employers' participation in the Fund; and
7. Fully reflect actuarial professional guidance and requirements in the advice given to the Administering Authority.

**A4 Other parties:-**

1. Investment advisers (either internal or external) should ensure the Fund's ISS remains appropriate, and consistent with this FSS;
2. Investment managers, custodians and bankers should all play their part in the effective investment (and dis-investment) of Fund assets, in line with the ISS;
3. Auditors should comply with their auditing standards, ensure Fund compliance with all requirements, monitor and advise on fraud detection, and sign off annual reports and financial statements as required;
4. Governance advisers may be appointed to advise the Administering Authority on efficient processes and working methods in managing the Fund;
5. Legal advisers (either internal or external) should ensure the Fund's operation and management remains fully compliant with all regulations and broader local government requirements, including the Administering Authority's own procedures;
6. The Department for Communities and Local Government (assisted by the Government Actuary's Department) and the Scheme Advisory Board, should work with LGPS Funds to meet Section 13 requirements.

## Appendix B – Regulatory framework

### B1 Why does the Fund need an FSS?

The Department for Communities and Local Government (DCLG) 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.

The requirement to maintain and publish a FSS is contained in LGPS Regulations which are updated from time to time. In publishing the FSS the Administering Authority has to have regard to any guidance published by Chartered Institute of Public Finance and Accountancy (CIPFA) (most recently in 2016) and to its Investment Strategy Statement.

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

### B2 Consultation and review

The LGPS Regulations requires the Fund to consult on its FSS. It is covered in more detail by the most recent CIPFA guidance, which states that the FSS must first be subject to “consultation with such persons as the authority considers appropriate”, and should include “a meaningful dialogue at officer and elected member level with council tax raising authorities and with corresponding representatives of other participating employers”.

In practice, for the Fund, the consultation process for this FSS was as follows:

- a) A draft version of the FSS was issued to all participating employers in November 2016 for comment;
- b) Comments were requested within 60 days;
- c) There was an Employers Forum on 30 January 2017 at which questions regarding the FSS could be raised and answered;
- d) Following the end of the consultation period the FSS was updated where required, approved by the Fund’s Pensions Committee in February 2017 then published in March 2017.

### B3 How is the FSS published?

The FSS is made available through the following routes:

- Published on the website, at: <http://www.yourpension.org.uk/Hertfordshire/Fund-information/Policy-statements.aspx>;
- A full copy is included in the annual report and accounts of the Fund <http://www.yourpension.org.uk/Hertfordshire/Fund-information/Annual-reports.aspx>;

#### **B4 How often is the FSS reviewed?**

The FSS is reviewed in detail at least every three years as part of the triennial valuation. This version is expected to remain unaltered until it is consulted upon as part of the formal process for the next valuation in 2019.

It is possible that (usually slight) amendments may be needed within the three year period. These would be needed to reflect any regulatory changes, or alterations to the way the Fund operates (e.g. to accommodate a new class of employer). Any such amendments would be consulted upon as appropriate:

- trivial amendments would be simply notified at the next round of employer communications,
- amendments affecting only one class of employer would be consulted with those employers,
- other more significant amendments would be subject to full consultation.

In any event, changes to the FSS would need agreement by the Pensions Committee and would be included in the relevant Committee Meeting minutes.

#### **B5 How does the FSS fit into other Fund documents?**

The FSS is a summary of the Fund's approach to funding liabilities. It is not an exhaustive statement of policy on all issues, for example there are a number of separate statements published by the Fund including the Investment Strategy Statement, Governance Compliance Statement and Communications Strategy Statement. In addition, the Fund publishes an Annual Report and Accounts with up to date information on the Fund.

These documents can be found on the web at: <http://www.yourpension.org.uk/Hertfordshire/Fund-information/Introduction.aspx>

## Appendix C - Actuarial assumptions

### C1 What are the actuarial assumptions?

These are expectations of future experience used to place a value on future benefit payments (“the liabilities”). Assumptions are made about the amount of benefit payable to members (the financial assumptions) and the likelihood or timing of payments (the demographic assumptions). For example, financial assumptions include investment returns, salary growth and pension increases; demographic assumptions include life expectancy, probabilities of ill-health early retirement, and proportions of member deaths giving rise to dependants’ benefits.

Changes in assumptions will affect the measured funding target. However, different assumptions will not of course affect the actual benefits payable by the Fund in future.

The combination of all assumptions is described as the “basis”. A more optimistic basis might involve higher assumed investment returns (discount rate), or lower assumed salary growth, pension increases or life expectancy; a more optimistic basis will give lower funding targets and lower employer costs. A more prudent basis will give higher funding targets and higher employer costs.

### C2 What basis is used by the Fund?

The Fund’s standard funding basis is described as the “ongoing basis”, which applies to most employers in most circumstances. This is described in more detail below. It anticipates employers remaining in the Fund in the long term.

However, in certain circumstances, typically where the employer is not expected to remain in the Fund long term, a more prudent basis applies: see [Note \(a\) to 3.3](#).

### C3 What assumptions are made in the ongoing basis?

#### a) Investment return / discount rate

The key financial assumption is the anticipated return on the Fund’s investments. This “discount rate” assumption makes allowance for an anticipated out-performance of Fund returns relative to long term yields on UK Government bonds (“gilts”). There is, however, no guarantee that Fund returns 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.

Given the very long-term nature of the liabilities, a long term view of prospective asset returns is taken. The long term in this context would be 20 to 30 years or more.

For the purpose of the triennial funding valuation at 31 March 2016 and setting contribution rates effective from 1 April 2017, the Fund actuary has assumed that future investment returns earned by the Fund over the long term will be 1.8% per annum greater than gilt yields at the time of the valuation (this is the same as that used at the 2013 valuation). In the opinion of the Fund actuary, based on the current investment strategy of the Fund, this asset out-performance assumption is within a range that would be considered acceptable for the purposes of the funding valuation.

**b) Salary growth**

Pay for public sector employees is currently subject to restriction by the UK Government until 2020. Although this “pay freeze” does not officially apply to local government and associated employers, it has been suggested that they are likely to show similar restraint in respect of pay awards. Based on long term historical analysis of the membership in LGPS funds, and continued austerity measures, the salary increase assumption at the 2016 valuation has been set to 0.9% below the retail prices index (RPI) per annum. This is a change from the previous valuation, which assumed 0.5% above RPI.

**c) Pension increases**

Since 2011 the consumer prices index (CPI), rather than RPI, has been the basis for increases to public sector pensions in deferment and in payment. Note that the basis of such increases is set by the Government, and is not under the control of the Fund or any employers.

As at the previous valuation, we derive our assumption for RPI from market data as the difference between the yield on long-dated fixed interest and index-linked government bonds. This is then reduced to arrive at the CPI assumption, to allow for the “formula effect” of the difference between RPI and CPI. At this valuation, we propose a reduction of 1.0% per annum. This is a larger reduction than at 2013, when a reduction of 0.8% was applied to the RPI assumption. This will serve to reduce the funding target (all other things being equal). (Note that the reduction is applied in a geometric, not arithmetic, basis).

**d) Life expectancy**

The demographic assumptions are intended to be best estimates of future experience in the Fund based on past experience of LGPS funds which participate in Club Vita, the longevity analytics service used by the Fund, and endorsed by the actuary.

The longevity assumptions that have been adopted at this valuation are a bespoke set of “VitaCurves”, produced by the Club Vita’s detailed analysis, which are specifically tailored to fit the membership profile of the Fund. These curves are based on the data provided by the Fund for the purposes of this valuation.

It is acknowledged that future life expectancy and, in particular, the allowance for future improvements in life expectancy, is uncertain. There is a consensus amongst actuaries, demographers and medical experts that life expectancy is likely to improve in the future. Allowance has been made in the ongoing valuation basis for future improvements in line with the 2013 version of the Continuous Mortality Investigation model published by the Actuarial Profession and a 1.25% per annum minimum underpin to future reductions in mortality rates. This is the same methodology as was adopted for the 2013 Valuation, but with updates to the underlying mortality tables.



**e) General**

The same financial assumptions are adopted for most employers, in deriving the funding target underpinning the Primary and Secondary rates: as described in (3.3), these calculated figures are translated in different ways into employer contributions, depending on the employer's circumstances.

The demographic assumptions, in particular the life expectancy assumption, in effect vary by type of member and so reflect the different membership profiles of employers.

## Appendix D - The calculation of Employer contributions

In [Section 2](#) a broad description of the way in which contribution rates are calculated was provided. This Appendix considers these calculations in much more detail. The calculations involve actuarial assumptions about future experience, and these are described in detail in Appendix C.

### D1 What is the difference between calculations across the whole Fund and calculations for an individual employer?

Employer contributions are normally made up of two elements:

- a) the estimated cost of ongoing benefits being accrued, referred to as the “Primary contribution rate” (see [C2](#) below); plus
- b) an adjustment for the difference between the Primary rate above, and the actual contribution the employer needs to pay, referred to as the “Secondary contribution rate” (see [C3](#) below).

The contribution rate for each employer is measured as above, appropriate for each employer’s funding position and membership. The whole Fund position, including that used in reporting to DCLG (see section 5), is calculated in effect as the weighted sum of all the individual employer rates. DCLG currently only regulates at whole Fund level, without monitoring individual employer positions.

### D2 How is the Primary contribution rate calculated?

The Primary element of the employer contribution rate is calculated with the aim that these contributions will meet the cost of current employees’ future benefit payments as they accrue. This is based upon the cost (in excess of members’ contributions) of the benefits which employee members earn from their service each year.

The Primary rate is calculated separately for all the employers, although employers within a pool will pay the contribution rate applicable to the pool as a whole. The Primary rate is calculated such that it is projected to:

1. meet the required funding target for all future years’ accrual of benefits\*, excluding any accrued assets,
2. within the determined time horizon (see [note 3.3 Note \(c\)](#) for further details),
3. with a sufficiently high probability, as set by the Fund’s strategy for the category of employer (see [3.3 Note \(e\)](#) for further details).

\* The projection is for the current active membership where the employer no longer admits new entrants, or additionally allows for new entrants where this is appropriate.

The projections are carried out using an economic modeller developed by the Fund’s actuary Hymans Robertson: this allows for a wide range of outcomes as regards key factors such as asset returns (based on the Fund’s investment strategy), inflation, and bond yields. The measured contributions are calculated such that the proportion of outcomes meeting the employer’s funding target (by the end of the time horizon) is equal to the required probability.

The approach includes expenses of administration to the extent that they are borne by the Fund, and includes allowances for benefits payable on death in service and on ill health retirement.

### **D3 How is the Secondary contribution rate calculated?**

The Fund operates the same target funding level for all employers of 100% of its accrued liabilities valued on the ongoing basis, unless otherwise determined (see [Section 3](#)). The Secondary rate is calculated as the balance over and above the Primary rate, such that the total is projected to:

1. meet the required funding target relating to past and future service benefit accrual
2. within the determined time horizon (see [3.3 Note \(c\)](#) for further details)
3. with a sufficiently high probability, as set by the Fund's strategy for the category of employer (see [3.3 Note \(e\)](#) for further details).

Therefore, when an employer is in deficit, the secondary rate will set out the additional contributions that are required to achieve a 100% funding level within an appropriate time horizon and with a sufficiently high probability. The secondary rate may be expressed as a percentage of pay or as a monetary amount per annum.

### **D4 What affects a given employer's valuation results?**

The results of these calculations for a given individual employer will be affected by:

1. past contributions relative to the cost of accruals of benefits;
2. different liability profiles of employers (e.g. mix of members by age, gender, service vs. salary);
3. the effect of any differences in the funding target, i.e. the valuation basis used to value the employer's liabilities;
4. any different time horizons;
5. the difference between actual and assumed rises in pensionable pay;
6. the difference between actual and assumed increases to pensions in payment and deferred pensions;
7. the difference between actual and assumed retirements on grounds of ill-health from active status;
8. the difference between actual and assumed amounts of pension ceasing on death;
9. the additional costs of any non ill-health retirements relative to any extra payments made; and/or
10. differences in the required probability of achieving the funding target.

### **D5 How is each employer's asset share calculated?**

The Administering Authority does not account for each employer's assets separately. Instead, the Fund's actuary is required to apportion the assets of the whole Fund between the employers, at each triennial valuation.

This apportionment uses the income and expenditure figures provided for certain cash flows for each employer. 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".

Actual investment returns achieved on the Fund between each valuation are applied proportionately across all employers, to the extent that employers in effect share the same investment strategy. 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, including but not limited to:

1. the actual timing of employer contributions within any financial year;
2. 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.

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 it considers that the Fund actuary's approach addresses the risks of employer cross-subsidisation to an acceptable degree.

## Appendix E – Key risks and controls

The Fund has an active risk management programme in place. Key risks are incorporated in the Fund's risk register which is monitored on an ongoing basis and reported to the Pensions Committee and LGPS Board on a quarterly basis.

Risk	Summary of Control Mechanisms
<p><b>The Pension Fund Investment Strategy does not deliver the long term projected investments returns and does not comply with legislation</b></p>	<p>Ensure the investment strategy complies with the Local Government Pension Scheme regulations, Investment Strategy Statement and Investment Management Agreements.</p>
	<p>Set the Investment Strategy in light of the Fund's solvency target and risk and return objectives and review at regular intervals to ensure the Strategy is still appropriate</p>
	<p>Diversify investment across asset classes and markets to reduce the impact of financial market volatility including setting a limit for the proportion of the Pension Fund's assets held in illiquid asset classes such as private equity and property and and keep the Fund's diversification policy under review.</p>
	<p>Establish limits for the maximum percentage of the total value of all investments in particular investments or classes of investment, within a prudential framework and after taking proper advice.</p>
	<p>Monitor and provide a quarterly report to the Pensions Committee on Investment Managers' performance against benchmark.</p>
	<p>Regularly review any assets that the Fund has previously determined should be held outside of the ACCESS pool, ensuring this continues to demonstrate value for money</p>
	<p>Monitor Investment Managers' compliance with the investment restrictions and limits laid out in the Pension Fund's Investment Strategy Statement and Investment Managers' Agreements and report any cases of non-compliance</p>
<p><b>The funding level of the Pension Fund deteriorates</b></p>	<p>Set investment out-performance targets at the triennial valuation with reference to the Pension Fund's current Investment Strategy and on a relatively prudent basis to reduce the risk of under-performance against anticipated returns. At the same time, review and agree the other actuarial assumptions such as salary increases, discount rates, longevity etc.</p>
	<p>Provide the Pensions Committee with quarterly actuarial reports that monitor the funding position of the Pension Fund and the sensitivity of this to changes in general market conditions.</p>
	<p>Monitor and ensure scheme employers pay the extra capital/strain cost of non ill-health retirements following each individual decision and in the year the decision is made.</p>
	<p>Monitor each scheme employer's ill-health experience on an ongoing basis against the "ill health budget" set for each employer at the triennial valuation and require them to make additional contributions to the Pension Fund where budgets are exceeded.</p>
	<p>Monitor cash flows at a whole Pension Fund level and an individual scheme employer level and certify secondary contributions as a monetary amount for those with reducing payrolls as identified at the triennial valuation.</p>

Risk	Summary of Control Mechanisms
	<p>At each triennial valuation, assign any liabilities relating to ceased transferee admission bodies to the original ceding scheme employer.</p> <p>Monitor the 'characteristics' and individual funding position of pool members to ensure pooling is still appropriate. Require members of the Schools or Parish and Town Councils Pools to sign a pooling agreement which sets certain conditions and requirements for scheme employers' participation in the pool.</p> <p>Set maximum time horizons after taking into account the particular characteristics of each type of scheme employer and the future working lifetime of its employees. Use shorter deficit recovery periods for organisations with a limited "life" in the Pension Fund or without statutory tax raising powers.</p> <p>Monitor the covenant of scheme employers and use a risk based approach for setting contribution strategies for employers.</p>
<p><b>Scheme employers default on meeting their obligations to the Pension Fund and LGPS</b></p>	<p>Develop data quality controls with the Pension Fund's third party pension's administration service to monitor membership data submitted by scheme employers to ensure it is accurate and up to date.</p> <p>Develop a risk evaluation approach to identify covenant risk, categorising scheme employers as low, medium or high. Establish a set of risk criteria and monitor scheme employers against this. Engage with scheme employers at an early stage to address funding issues.</p> <p>Monitor contributions to ensure that scheme employers are paying the correct employer contribution rate to agreed deadlines.</p> <p>Do not allow unsupported employers to be admitted to the Pension Fund. Require all community admission bodies and transferee admission bodies to obtain a bond or guarantor from a scheme employer. Revalue bonds every three years to ensure the risk cover is still appropriate.</p> <p>Carry out regular financial checks on participating scheme employers, especially non-tax raising bodies.</p> <p>Carry out an annual employer survey to identify any changes in funding stream for scheme employers.</p> <p>Pool the contributions for scheme employers with similar characteristics to allow sharing of risk amongst scheme employers.</p> <p>Carry out cessation valuations on a more prudent gilts basis to ensure the payment calculated when a scheme employer's liabilities are crystallised is sufficient to meet the future payment of benefits made by the Pension Fund.</p>
<p><b>The Pension Fund and its third party providers do not comply with regulations, statute or procedure</b></p>	<p>Review the Custodian's and Investment Managers' internal control reports to identify any concerns over controls and processes in place</p> <p>Ensure the Custodian undertakes monthly reconciliations with the Pension Fund's Investment Managers to ensure all assets are correctly accounted for and holdings are agreed.</p> <p>Require all large employers in the Pension Fund to provide an Annual Assurance Certification that payroll systems are compliant and have been tested by the scheme employers' internal auditors</p>

Risk	Summary of Control Mechanisms
	Take advice from Fund Actuary on position of Fund as at prior valuation, and consideration of proposed valuation approach relative to anticipated Section 13 analysis.
	Engage data matching service to receive earlier notifications of entitlement changes.
	Take proper advice to ensure a regulatory compliant asset pool in operation by statutory deadlines.
	Work in conjunction with the Strategic Procurement Group to ensure all procurements are carried out in accordance with HCC contract and EU regulations.
	Review the Pension Fund SORP in preparing the Statement of Accounts to ensure compliance and engage external audit to review the Pension Fund accounts each year.
	Manage performance of the Pension Fund's third party pension's administration service through a service level agreement and monitor against Key Performance Indicators.
	Work closely with the Pension Fund's third party pension's administration service to ensure it complies with current regulations and is alert to and can implement any changes to scheme benefits.
	Ensure the Pension Fund's third party pension's administration service has a robust programme in place to test controls on the membership benefit system and that they are fully compliant and up to date.
	Engage internal and external audit reports to regularly test that appropriate controls are in place over the payment of benefits and expenses and collection of contributions and that they are working effectively. Implement any recommendations resulting from both these audits.

## Appendix F – Glossary

<b>Actuarial assumptions/basis</b>	The combined set of assumptions made by the actuary, regarding the future, to calculate the value of the funding target. The main assumptions will relate to the discount rate, salary growth, pension increases and longevity. More prudent assumptions will give a higher target value, whereas more optimistic assumptions will give a lower value.
<b>Administering Authority</b>	The council with statutory responsibility for running the Fund, in effect the Fund's "trustees".
<b>Admission Bodies</b>	Employers where there is an Admission Agreement setting out the employer's obligations. These can be Community Admission Bodies or Transferee Admission Bodies. For more details (see <a href="#">2.3</a> ).
<b>Covenant</b>	The assessed financial strength of the employer. A strong covenant indicates a greater ability (and willingness) to pay for pension obligations in the long run. A weaker covenant means that it appears that the employer may have difficulties meeting its pension obligations in full over the longer term.
<b>Designating Employer</b>	Employers such as town and parish councils that are able to participate in the LGPS via resolution. These employers can designate which of their employees are eligible to join the Fund.
<b>Discount rate</b>	The annual rate at which future assumed cashflows (in and out of the Fund) are discounted to the present day. This is necessary to provide a funding target which is consistent with the present day value of the assets. A lower discount rate gives a higher target value, and vice versa. It is used in the calculation of the Primary and Secondary rates.
<b>Employer</b>	An individual participating body in the Fund, which employs (or used to employ) members of the Fund. Normally the assets and funding target values for each employer are individually tracked, together with its Primary rate at each valuation.
<b>Funding target</b>	The actuarially calculated present value of all pension entitlements of all members of the Fund, built up to date. This is compared with the present market value of Fund assets to derive the deficit. It is calculated on a chosen set of actuarial assumptions.
<b>Gilt</b>	A UK Government bond, ie a promise by the Government to pay interest and capital as per the terms of that particular gilt, in return for an initial payment of capital by the purchaser. Gilts can be "fixed interest", where the interest payments are level throughout the gilt's term, or "index-linked" where the interest payments vary each year in line with a specified index (usually RPI). Gilts can be bought as assets by the Fund, but their main use in funding is as an objective measure of solvency.
<b>Guarantee / guarantor</b>	A formal promise by a third party (the guarantor) that it will meet any pension obligations not met by a specified employer. The presence of a guarantor will mean, for instance, that the Fund can consider the employer's covenant to be as strong as its guarantor's.



<b>Letting employer</b>	An employer which outsources or transfers a part of its services and workforce to another employer (usually a contractor). The contractor will pay towards the LGPS benefits accrued by the transferring members, but ultimately the obligation to pay for these benefits will revert to the letting employer. A letting employer will usually be a local authority, but can sometimes be another type of employer such as an Academy.
<b>LGPS</b>	The Local Government Pension Scheme, a public sector pension arrangement put in place via Government Regulations, for workers in local government. These Regulations also dictate eligibility (particularly for Scheduled Bodies), members' contribution rates, benefit calculations and certain governance requirements. The LGPS is divided into 101 Funds which map the UK. Each LGPS Fund is autonomous to the extent not dictated by Regulations, e.g. regarding investment strategy, employer contributions and choice of advisers.
<b>Maturity</b>	A general term to describe a Fund (or an employer's position within a Fund) where the members are closer to retirement (or more of them already retired) and the investment time horizon is shorter. This has implications for investment strategy and, consequently, funding strategy.
<b>Members</b>	The individuals who have built up (and may still be building up) entitlement in the Fund. They are divided into actives (current employee members), deferreds (ex-employees who have not yet retired) and pensioners (ex-employees who have now retired, and dependants of deceased ex-employees).
<b>Primary contribution rate</b>	The employer contribution rate required to pay for ongoing accrual of active members' benefits (including an allowance for administrative expenses). See Appendix D for further details.
<b>Profile</b>	The profile of an employer's membership or liability reflects various measurements of that employer's members, ie current and former employees. This includes: the proportions which are active, deferred or pensioner; the average ages of each category; the varying salary or pension levels; the lengths of service of active members vs their salary levels, etc. A membership (or liability) profile might be measured for its maturity also.
<b>Rates and Adjustments Certificate</b>	A formal document required by the LGPS Regulations, which must be updated at least every three years at the conclusion of the formal valuation. This is completed by the actuary and confirms the contributions to be paid by each employer (or pool of employers) in the Fund for the three year period until the next valuation is completed.
<b>Scheduled Bodies</b>	Types of employer explicitly defined in the LGPS Regulations, whose employers must be offered membership of their local LGPS Fund. These include Councils, colleges, universities, academies, police and fire authorities etc, other than employees who have entitlement to a different public sector pension scheme (e.g. teachers, police and fire officers, university lecturers).
<b>Secondary contribution rate</b>	The difference between the employer's actual and Primary contribution rates. In broad terms, this relates to the shortfall of its asset share to its funding target.

<b>Stabilisation</b>	Any method used to smooth out changes in employer contributions from one year to the next. This is very broadly required by the LGPS Regulations, but in practice is particularly employed for large stable employers in the Fund. Different methods may involve: probability-based modelling of future market movements; longer deficit recovery periods; higher discount rates; or some combination of these.
<b>Valuation</b>	An actuarial investigation to calculate the liabilities, future service contribution rate and common contribution rate for a Fund, and usually individual employers too. This is normally carried out in full every three years (last done as at 31 March 2016), but can be approximately updated at other times. The assets value is based on market values at the valuation date, and the liabilities value and contribution rates are based on long term bond market yields at that date also.

## **INVESTMENT STRATEGY REVIEW**

### Report of the Director of Resources

Author of the report: Patrick Towey, Head of Specialist Accounting  
(Telephone: 01992 555148)

#### **1. Purpose of the Report**

- 1.1 To inform the Pension Committee of the process and timetable for the review of the Fund's investment Strategy.

#### **2. Summary**

- 2.1 New investment regulations introduced by the Government require each administering authority to produce and publish new investment strategy statements by 1<sup>st</sup> April 2017.
- 2.2 The new investment strategy statement (ISS) replaces, and largely replicates the current Statement of Investment Principles (SIP). The ISS will be required to cover a number of areas, specifically:
- A requirement to invest money in a wide range of investments;
  - The authority's assessment of the suitability of particular investments and types of investments;
  - The authority's approach to risk, including the ways in which risks are to be measured and managed;
  - The authority's approach to pooling investments;
  - The authority's policy on environmental, social and governance (ESG) considerations and how they affect investment decision making;
  - The authority's policy with regard to the stewardship of assets, including the exercise of voting rights; and
  - The maximum percentage authorities deem should be allocated to different asset classes or types of investment.
- 2.3 The new regulations and guidance provides a prudential framework within which investment strategy can be implemented and managed and is less prescriptive than the current regulations.
- 2.4 The new regulations also support the Government's intention to progress the pooling of investments and authorities will be required to report progress on transitioning assets towards the pool against implementation plans.

- 2.5 The regulations also enable the Secretary of State the power of intervention and issue direction if he is satisfied that an administering authority is failing to act in accordance with the guidance.
- 2.6 Whilst this is largely a refresh of our current investment strategy, the key areas that will require a focussed piece of work will be:
- the authority's policy on ESG and consideration of non-financial factors when selecting, retaining and realising investments and we engage over the longer term;
  - does the current risk and return objectives still apply in determining asset allocation and the mix of growth and defensive assets; and
  - how we weave the requirements of asset pooling into the revised IS.

2.6 In anticipation of the introduction of these new regulations, which come into effect 1<sup>st</sup> November 2016, the Fund's investment consultant Nick Sykes, Mercer presented a recap of the Fund's current investment strategy at this committee's meeting on 9<sup>th</sup> September. The Mercer paper also set out a plan for the review of the ISS and that the actuarial valuation results will inform the review by answering the following questions:

- Is the 65/35 growth/defensive asset allocation split still appropriate?
- Are the allocations within the growth and low risk portfolios appropriate?
- Should new asset classes be considered?

Now that we have the initial valuation results we can develop the work that Nick Sykes started when recapping the IS with the objective of having a new investment strategy in place by the 1<sup>st</sup> April 2017.

2.7 Officers will work with Mercer to review the strategy and bring a draft investment strategy to the Pension Committee on 24 February 2017, for initial review and discussion; this will be a focussed piece of work for this particular committee agenda. If further amendments are required then a revised draft will come to the Pension Committee on 31 March 2017 for final review and agreement.

### **3. Recommendations**

3.1 That the Pensions Committee notes the content of this report and agrees the plan for the review of the Fund's investment strategy.

### **4. Investment Strategy**

4.1 This section provides a summary of the requirements that an Administering Authority must consider when reviewing and setting its investment strategy under the new regulations. Although the new regulations are less prescriptive there are new powers of intervention that the Secretary of State may use through issuing a direction to an administering authority

where there is evidence to suggest that an administering authority is acting unreasonably.

#### **4.2 Directions by the Secretary of State**

One of the main aims of the new investment regulations will be to transfer investment decisions and their consideration more fully to administering authorities. The new regulations relax the regulatory framework and have less central prescription and limits for asset allocation. However, the new regulations introduce a safeguard to ensure that administering authorities act appropriately when using the less prescriptive approach to set and maintain their local IS. Where there is evidence that an authority has acted unreasonably then the Secretary of State may consider intervention but only where this is justified and where the relevant parties have been consulted.

#### **4.3 Investment of money in a wide variety of investments**

When setting its IS the regulations recommend that Funds have a properly diversified portfolio of assets to reduce overall portfolio risk. When preparing and maintaining a policy on asset diversification, administering authorities:-

- Must take proper advice;
- Must set out clearly the balance between different types of investments;
- Must identify the risks associated with their overall investment strategy; and
- Must periodically review their policy to mitigate against any such risks.

The Hertfordshire Fund has a diversified portfolio of assets and asset allocation is reviewed regularly and will be reviewed again when setting and agreeing the new IS.

#### **4.4 Suitability of particular investments and types of investments**

Funds will need to consider the suitability of individual investment classes and this will vary according to each Fund's funding and investment policies. When preparing a policy on the suitability of particular investments and types, the regulations state that administering authorities:-

- Must take proper advice;
- Should ensure that asset allocation policy is compatible with achieving their locally determined solvency target; and
- Must review periodically the suitability of their investment portfolio to ensure that returns, risk and volatility are all appropriately managed and are consistent with their overall IS.

The Hertfordshire Fund ensures funds are suitably invested and reviews and monitors its investment allocation regularly. The valuation results will inform this piece of work and whether we want to de-risk further i.e. move to more

defensive asset classes if the funding level has improved since the last valuation.

#### **4.5 Approach to risk, including the ways in which risks are to be measured and managed.**

Every administering authority will have a different approach to the risk it takes when it sets its IS and this will be dependent on its funding level and its appetite for risk. The requirements set out in the guidance state that administering authorities:-

- Must take proper advice;
- State clearly their appetite for risk;
- Should be aware of the risks that may impact on their overall funding and investment strategies;
- Should take measures to counter those risks;
- Should periodically review the assumptions on which their investment strategy is based; and
- Should form contingency plans to limit the impact of risks that might materialise.

This Fund when it last reviewed its IS agreed its appetite for risk against its investment objectives and set an appropriate risk budget. The Fund's appetite for risk will be reviewed and refreshed as part of this IS review. At the pension committee meeting on the 9<sup>th</sup> September, Nick Sykes gave this committee a recap of the current IS and questions to be considered in the review of the Fund's strategy.

#### **4.6 Approach to pooling investments, including the use of collective investment vehicles and shared services**

This new regulation requires administering authorities to set out their approach to pooling and the proportion of assets that will be invested through the pool. The requirements of this regulation are summarised below:

- Confirm the pooling arrangements meet the criteria set out in the November 2015 investment reform and criteria guidance;
- Set out the proportion of assets to be invested through pooling;
- Set out the structure and governance arrangements of the pool and the mechanisms by which the authority can hold the pool to account;
- Set out the services that will be shared or jointly procured;
- Provide a summary of assets it intends to hold outside the pool along with the rationale and how it demonstrates value for money;
- Regularly review assets that the authority has previously determined should be held outside of the pool, ensuring this continues to demonstrate value for money; and
- Submit an annual report on the progress of asset transfers to the Scheme Advisory Board.

As a member of the ACCESS pool, the Hertfordshire Fund has shown its commitment to pooling and is working with fellow ACCESS members on ensuring that effective governance arrangements are put in place to hold the pool to account. As part of the establishment of the ACCESS pool a detailed plan has been established to develop the governance of the pool, the procurement of the operator and legal advisor, and the establishment of tax efficient sub-funds for managing the ACCESS Funds' assets. The ACCESS pool work will inform this piece of the Strategy and ACCESS officers who share Mercer as an investment consultant are meeting in December to address this piece of the strategy.

#### **4.7 How environmental, social, or corporate governance considerations are taken into account in the selection, non-selection, retention and realisation of investments.**

This regulation requires administering authorities to consider any factors that are financially material to the performance of their investments, including social, environmental and corporate governance factors. In preparing its policy on ESG, an administering authority:-

- Must take proper advice;
- Should explain the extent to which the views of their local pension board and other interested parties who they consider may have an interest will be taken into account when making an investment decision based on non-financial factors;
- Must explain the extent to which non-financial factors will be taken into account in the selection, retention and realisation of investments;
- Should not pursue policies that are contrary to UK foreign policy or UK defence policy; and
- Should explain their approach to social investments.

This guidance is stronger than previous regulations on addressing issues of responsible investment and encourages engagement as a tool for long-term investors. This will be a focussed piece of work that officers, Mercers and members will need to work together to develop an approach for the Hertfordshire Fund.

#### **4.8 The exercise of rights (including voting rights) attaching to investments.**

This regulation encourages administering authorities to consider the best way to engage with companies to promote their long-term success, either directly, in partnership with other investors or through their investment managers, and explain their policy on stewardship with reference to the Stewardship Code. In preparing its policy on the exercise of rights, administering authorities:

- Must give a reason in their Investment Strategy Statement for not adopting a policy of exercising rights, including voting rights, attaching to investments;

- Should, where appropriate, explain their policy on stewardship with reference to the stewardship code;
- Should strongly encourage their fund managers to vote their company shares in line with their policy;
- May wish to appoint an independent proxy voting agent to exercise this proxy voting and monitor the voting activity of the managers; and
- Should publish a report of voting activity as part of their pension fund annual report.

The Hertfordshire Fund engages the services of Institutional Shareholder Services (ISS) to instruct its managers how to vote at the annual general and extraordinary general meetings of the top 350 UK FTSE listed companies. A report is submitted annually to this Committee setting out breaches of voting policy, the next annual report will come to this committee in February 2017. The Hertfordshire Fund is also a member of the Local Authority Pension Fund Forum (LAPFF), a body which engages on behalf of its members with companies on environmental, social and governance matters. As part of the review of the IS, this piece of work will be about formalising what we have in place at the moment and adapting it for the purposes of the regulations.

## **5. Next Steps**

- 5.1 The Fund's officers will work with Mercer to review the current investment strategy in light of the new investment regulations and taking into consideration the outcome of the Fund valuation results and bring to this Committee in February 2017 a draft for consideration and comment. Subject to any further amendments a final investment strategy will come back to this committee in March 2017 for final sign off.
- 5.2 As part of the review and final sign off of the investment strategy, the draft IS will also go to the Pension Board for comment at its meeting in February 2017.

### References:

Regulation 7 of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016.



**PENSION FUND ASSET POOLING – ACCESS UPDATE**

*Report of the Director of Resources*

Author of the report: Patrick Towey Head of Specialist Accounting (Telephone: 01992 555148)

**1. Purpose of the Report**

- 1.1 To provide the Pensions Committee with an update on recent ACCESS pool developments and the ACCESS Chairmen engagement meeting that took place on 13 October 2016.

**2. Summary**

- 2.1 The ACCESS pool proposal for the pooling of assets was submitted to Government by the deadline date of the 15 July 2016. The Government was expected to review all pool submissions and inform all pools of their decision in September; however, at the time of writing this report none of the pools have received any formal decision from the Government.
- 2.2 At a National cross pool meeting held on the 20 October a representative from Department for Communities and Local Government (DCLG) informed the pools that the Minister for Local Government, Marcus Jones MP, would like to meet representatives from each pool to discuss their pool submission, the timetable and progress to delivery of the pool, and the political buy-in to each pool. The Minister, in particular, is keen to meet elected Members; a deputation from the ACCESS pool will meet the Minister at some time in November, and a representative of the Hertfordshire Fund will be present at this meeting. A verbal briefing will be provided to members of this Committee if this meeting takes place before this Pension Committee meeting.
- 2.2 Following the decision by all ACCESS Funds to rent an operator, with the option to build in the future, the main focus of work by ACCESS has been the development of the governance of the pool and how local Fund asset allocation decisions will be implemented through the pool operator via a Joint Governance Committee (JGC). To enable this JGC to implement local Fund asset allocations, an Inter Authority Agreement will need to be put in place by the end of March 2017 and this will require sign off by each administering authority through their individual constitutional process. The deadline is considered challenging as this change will require approval by Council, and most of the ACCESS Councils will only have their February budget meetings

to agree this constitutional change.

- 2.3 Legal officers representing the Funds in the ACCESS pool have been involved in the process for establishing an inter authority agreement. Eversheds have been appointed to provide the first draft of the heads of terms for this agreement for discussion and agreement by Fund legal officers prior to the next ACCESS Chairmen meeting in December. The inter authority agreement will be put before this Committee at its meeting on the 24 February 2017 for comment and to recommend its approval by full Council at its meeting on 21 March 2017.
- 2.4 At the most recent ACCESS Chairmen meeting on 13 October, the ACCESS Chairmen during its governance discussion considered the establishment of an independent non-voting Chairman to sit on the Joint Governance Committee. This was put to a vote by the meeting and the proposal was rejected by 9 votes to 2. Hertfordshire were one of the only two authorities in favour of an independent Chair.
- 2.5 ACCESS officers will hold engagement days with potential operators in November to understand the depth of the operator marketplace and to inform the specification for the OJEU procurement. The Hertfordshire Fund is leading on the procurement of a legal advisor to assist the ACCESS pool in the procurement of a regulated third party provider, the operator, and specific legal advice on the establishment of tax efficient sub-funds for the management of Fund assets. The legal advisor will also be asked to provide advice on new or replacement contracts with investment managers: and transition plans for the phased transfer of assets to the pool. The procurement process will take up to 8 weeks.

### **3. Recommendations**

- 3.1 That the Pensions Committee notes the content of this report.