BRENT COUNCIL	**Pension Fund Sub Committee** 1st March 2011 **Report from the Director of Finance and Corporate Services**
For Action	Wards Affected: ALL
	2010 ACTUARIAL VALUATION OF THE BRENT PENSION FUND

1 SUMMARY

This report outlines the anticipated results of the Actuarial Valuation as at 31st March 2010, which indicates that the employers' contribution rates will rise. The actuary will attend the meeting of the Sub Committee to present their findings in more detail.

2 RECOMMENDATIONS

Members are asked to:-

a) Note the anticipated results of the 2010 Actuarial Valuation.

3 DETAIL

Background to the 2010 Actuarial Valuation

3.1 The Brent Pension Fund actuary, Aon Hewitt Ltd, is required to value the assets and liabilities of the fund every three years to determine its financial health. The assets of the fund are the equities, bonds, property, alternative investments (hedge fund, private equity, Global Tactical Asset Allocation, and infrastructure) and cash owned by the fund. The liabilities are the current and future pensions and lump sums owed to pensioners, deferred pensioners and active members. If the actuary finds that the assets may not be sufficient to meet liabilities when due, employers' contributions may be increased. If assets will be more than sufficient to meet liabilities, employers' contributions may be decreased. Employee contributions currently vary between 5.5% and 7.5%, depending on pay levels.

3.2 The 2007 Actuarial Valuation revealed the assets of the fund covered 72% of liabilities (from 67% in 2004). The main reasons for the improvement in the funding level were:-

a) Good investment returns during the period 2004/07. The Fund grew in value from £344m to £498m, however the deficit grew from £174m to £193.5m.
b) The impact of higher contributions designed to eliminate the deficit by 2033.
c) Changes in the advance credit taken for future investment returns (the discount rate) of 0.25% per annum consistent with asset allocation changes made between 2004 and 2007.

These were partially offset by:-

d) A higher allowance for future improvements in longevity – experience since 2004 suggested that pensioners are living longer than previously expected, increasing the cost of benefits.
e) Expectations for price inflation derived from the gilt market were higher than in 2004 (by 0.3% per annum).
f) Costs were increased by delays in implementing provisions for later retirement and by the recycling of 50% of savings into the new scheme.

3.3 The impact on employer contribution rates varied depending on individual employer circumstances. While rates for Brent Council remained stable, those for Brent Housing Partnership and the College of North West London fell, while those for admitted bodies rose. It should also be noted that the Valuation did not reflect the sharp deterioration in investment markets from mid 2007, though the actuary noted that if the deterioration was not reversed there would be adverse implications for the next Valuation.

2010 Actuarial Valuation

3.4 The 2010 Actuarial Valuation indicates a deterioration in the funding position since 2007. The Fund has declined in value (from £499m to £456m), the deficit has grown (from £193.5m to £295.4m) and the funding ratio fallen (from 72% to 61%). The 2007 discount rate assumed that assets would return 6.45% per annum, but instead equity markets fell sharply between 2007 and 2009.

3.5 The main factors affecting the Valuation are as follows:-

a) Negative - Poor investment returns.
b) Negative - Longevity. Staff are living longer as diets and health care improve.
c) Negative – Reducing payroll will mean fewer active members to contribute towards reducing the pension fund deficit.

d) Negative - Price inflation. The 2007 Valuation assumed RPI inflation of 3.2% per annum, but inflation is above that level (RPI is currently 5.1%), and future expectations are rising.
e) Positive – The government has announced that, in future, pension increases will be calculated using the Consumer Prices Index (CPI) rather than the Retail Prices Index (RPI). As the CPI has generally been considerably less than the RPI over the period of measurement (by an average of 0.7% per annum), the value of past service and future benefits has been reduced. This has meant that the funding level has improved slightly whilst the future service rate (the cost of providing for future service) has fallen.
f) Positive – The allowance for future investment returns (the discount rate) for long term Scheduled Bodies has been increased further. (There is less flexibility to do this for most admission bodies who may leave the Fund at any time.

3.6 The overall impact of the points above has reduced overall future service contribution rates slightly, but increased the deficit, and hence the contributions required to eliminate this over 25 years. The overall level of contributions has therefore increased slightly. Contributions for individual employers depend on their own particular circumstances.

3.7 However, the actuary has also been very concerned that progress in reducing the deficit would have been impeded by falling payrolls as local authorities, colleges and charities seek to manage the stark economic environment and falling revenues from government. The actuary has therefore expressed the target employer contributions as the sum of:-

a) a percentage (to cover the future service rate) plus
b) a monetary amount in each year to reduce the deficit.

Brent, as administering authority, will monitor future contributions to ensure that these target contributions are being met, and may need to increase rates further if contributions are too low in early years.

3.8 Converting the annual deficit amounts each year into estimated percentages of pay, on the basis of future payroll assumptions, the estimated impact on employers' contribution rates (excluding contractors) expressed as a percentage of pay is as follows:-

	2010/11	**2011/12**	**2012/13**	**2013/14**
	%	**%**	**%**	**%**
Brent Council and schools (S)	22.9	25.1	26.9	27.4
Brent Housing Partnership (S)	14.1	15.8	15.8	15.8
North West London College (S)	18.2	20.4	20.4	20.4
National Autistic Society (A)	23.7	26.4	32.1	37.7
Other Admitted Bodies (A)	20.1	23.5	23.5	23.5

The contributions payable by each employer are subject to confirmation by the actuary and may change.

3.9 The following points should be noted:-

a) For Brent Council the increase in contribution rates suggested by the 2010 Valuation is being phased in over six years. It is therefore anticipated that rates may need to rise further (after 2013/14). However, this will depend on revised regulations following the implementation of the Hutton review including potential increases to employee contribution rates as well as the Fund's experiences over the next three years. If future developments are favourable for the Fund's finances further increases may not be necessary
b) Brent Association for the Disabled is being treated on a standalone basis as there is only one active member of the Local Government Pension Scheme.
c) The Ark Academy, as a new Scheduled Body (S above) is being treated as a standalone body as it did not inherit a deficit.

Other issues arising from the Valuation

3.10 There is a case for considering raising the proportion of the fund invested in bonds (currently 18%) to safeguard income to pay benefits. A number of private sector funds have reviewed their asset allocation to increase the match to liabilities, which helped their performance during the market turmoil of 2007-09, but reduced comparative returns during the equity rally since March 2009. It can be argued that local authority funds have a longer investment horizon than their private sector counterparts, and can maintain a higher weighting in equities and other real assets. It is also apparent that gilts are currently very expensive, reflecting low interest rates, and yield low income. Gilts may also fall in price. An alternative route may be to increase exposure to other assets that have lower volatility and better prospective returns than bonds, such as hedge funds, infrastructure or (possibly) currency. It is suggested that changes to asset allocation await the review planned for 2011.

3.11 Brent Council, as Administering Authority for the Fund, is required to produce a Funding Strategy Statement (FSS) to reflect how the fund will meet its liabilities as the fall due. A revised draft FSS is attached as Appendix 1. The draft continues to reflect the 25 year recovery period (though it permits some flexibility up to 30 years), and has some changes to reflect the grouping of admitted bodies, the requirement for a bond as security if a body fails, and recognition that admitted bodies may struggle if employer rates are increased sharply. The draft has been circulated to employers and any responses will be communicated orally at the meeting.

4 FINANCIAL IMPLICATIONS

The Valuation will result in increased employers' contributions to the pension fund.

5 STAFFING IMPLICATIONS

None directly.

6 DIVERSITY IMPLICATIONS

The proposals in this report have been subject to screening and officers believe that there are no diversity implications arising from it.

7 LEGAL IMPLICATIONS

There are no legal implications arising from the report.

8 BACKGROUND

Aon Hewitt - Draft Actuarial Valuation papers 2010

Persons wishing to discuss the above should contact the Exchequer and Investment Section, Finance and Corporate Resources, on 0208 937 1472/74 at Brent Town Hall.

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