



Government Actuary's Department



Local Government Pension Scheme Northern Ireland

Review of the actuarial valuation as at 31 March 2016 pursuant to
Section 13 of the Public Service Pensions Act (Northern Ireland) 2014

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1 Executive Summary

- 1.1 The Government Actuary has been appointed by the Department for Communities (DfC) to report under section 13 of the Public Service Pensions Act (Northern Ireland) 2014 in connection with the actuarial valuations of the Local Government Pension Scheme Northern Ireland pension fund ("LGPS NI" or "the Scheme").
- 1.2 Section 13 requires the Government Actuary to report on compliance, consistency, solvency and long-term cost efficiency in respect of the actuarial valuation of the Scheme.
- 1.3 This is the first section 13 report for LGPS NI. This report is based on the 2016 actuarial valuation of the LGPS NI pension fund, other data provided by Northern Ireland Local Government Officers' Superannuation Committee (NILGOSC) and its actuary. We are grateful to these stakeholders for their assistance in preparing this report.
- 1.4 We have concluded that the 2016 actuarial valuation of LGPS NI and the resulting employer contribution rates achieve the aims set out in Section 13 in respect of compliance, consistency, solvency and long-term cost efficiency. We have therefore not recommended any remedial steps in this report.
- 1.5 The following paragraphs provide further details on compliance, consistency, solvency and long-term cost efficiency, including a few suggestions that DfC and NILGOSC may wish to note.

Compliance

- 1.6 Our review indicated that LGPS NI fund valuation was compliant with relevant regulations on the basis described in Chapter 3 of this report.

Consistency

- 1.7 As there is only one fund in LGPS NI, there are no other actuarial valuations in respect of LGPS NI to compare with.

Solvency

- 1.8 The solvency requirement is that employer contributions should be set at such a level as to ensure that the scheme's liabilities can be met as they arise.
- 1.9 In our view, LGPS NI pension fund meets the conditions required to be able to demonstrate solvency. The fund is in a strong financial position; the funding level compares well with the LGPS England and Wales funds.
- 1.10 Our engagement with NILGOSC gave us reassurance that the fund is aware of the risks we have identified in this report and has processes in place to manage and mitigate them. The risks identified include those that follow.



Volatility of employer contribution

- 1.11 Solvency is dependent on employers being able to pay contributions as required, knowing that these contributions may increase or decrease significantly in future. LGPS NI has significant proportion of return seeking assets, which is typical of most LGPS funds. Changes to the value of scheme assets may place upward or downward pressure on employer contribution rates. This risk is included in NILGOSC's funding strategy statement and it is actively managed: in 2017, NILGOSC undertook a review of its strategic funding target and its target asset allocation, and moved to a less risky portfolio.
- 1.12 NILGOSC might want to consider whether any further actions are needed to communicate the risk of employer contribution volatility to stakeholders, including employers.

High proportion of non-statutory employers

- 1.13 LGPS NI has a high proportion of non-Statutory employers (eg Housing Associations, Universities, Colleges, Schools). If such employers exit the scheme and it is not possible to obtain all or part of the exit payment due from them, costs fall back on the other scheme employers. This risk is included in NILGOSC's funding strategy statement and it is actively managed: NILGOSC carries out triennial assessment of employer covenant and acts to change employer contribution rates where necessary.
- 1.14 We understand that, at triennial valuations, NILGOSC's actuary provides the exit payment that would be due from each employer (if they were to have exited on the valuation date). NILGOSC may wish to consider monitoring these figures as part of its process for managing this risk.

Long term cost efficiency

- 1.15 The rate of employer contributions should be sufficient to make provision for the cost of current benefit accrual, with an appropriate adjustment to that rate for any surplus or deficit in the fund.
- 1.16 In our view, LGPS NI pension fund meets the conditions required to be able to demonstrate long-term cost efficiency of the scheme.
- 1.17 At the 2016 valuation, employer contribution rates increased and the deficit recovery period changed from 2014-34 to 2017-37. The length of the deficit recovery period was 20 years in both cases, and the deficit recovery end point moved back from 2034 to 2037. We have no concerns about this in the context of increasing employer contribution rates.
- 1.18 We would not normally expect to see employer contribution rates decreasing (reducing the burden on current taxpayers) at the same time as the deficit recovery end point being extended further into the future (increasing the burden on future taxpayers). If at a future valuation it was possible for employer contributions to be reduced, we suggest that NILGOSC consider maintaining the deficit recovery end point (or moving it forwards), rather than moving it backwards.



2 Introduction

The Local Government Pension Scheme Northern Ireland and fund valuation

- 2.1 The LGPS NI is a funded scheme governed by the Local Government Pension Scheme Regulations (Northern Ireland) 2014¹ (the 'Regulations'). The Scheme provides pensions and other benefits to employees who have worked in local government or for other Scheme employers, and to their dependants. The Scheme is managed and administered locally by the Northern Ireland Local Government Officers' Superannuation Committee ('NILGOSC')². NILGOSC must obtain an actuarial valuation of the scheme under Regulation 68 of the Regulations. Employer contributions are payable in accordance with the rates and adjustments certificate issued alongside the actuarial valuation.
- 2.2 The latest valuation of the LGPS NI under Regulation 68 was as at 31 March 2016. The valuation report³ was signed on 29 March 2017.
- 2.3 This report was prepared in accordance with the Funding Strategy Statement⁴ which is prepared, maintained and published by NILGOSC under the Regulations.

GAD's review and section 13

- 2.4 Section 13 applies for the first time to the valuation as at 31 March 2016.
- 2.5 Subsection (4) of section 13 requires the Government Actuary (as the person appointed by DfC) to report on whether the four main aims are achieved, namely:
- > Compliance: whether the fund's valuation is in accordance with the scheme regulations
 - > Consistency: whether the fund's valuation has been carried out in a way which is not inconsistent with the other fund valuations within LGPS NI
 - > Solvency: whether the rate of employer contributions is set at an appropriate level to ensure the solvency of the pension fund
 - > Long term cost efficiency: whether the rate of employer contributions is set at an appropriate level to ensure the long-term cost-efficiency of the scheme, so far as relating to the pension fund
- 2.6 Section 13 subsection (6) states that if any of the aims of subsection (4) are not achieved:
- a) the report may recommend remedial steps;

¹ SR 2014 No 188

² As established by under section 1 of the Local Government (Superannuation) Act (Northern Ireland) 1950 and subject to the requirements of Schedule 3 of the Regulations.

³ https://www.nilgosc.org.uk/DatabaseDocs/new_5983015_northern_ireland_lgps_-_actuarial_valuation_as_at_31_march_2016.pdf

⁴ <https://www.nilgosc.org.uk/DataEditorUploads/Pension%20Fund/Final%20FSS%20Sept%202016.pdf>



- b) the scheme manager must—
 - (i) take such remedial steps as the scheme manager considers appropriate, and
 - (ii) publish details of those steps and the reasons for taking them;
- c) the responsible authority may—
 - (i) require the scheme manager to report on progress in taking remedial steps;
 - (ii) direct the scheme manager to take such remedial steps as the responsible authority considers appropriate.

2.7 This report is addressed to DfC as the responsible authority for the purposes of subsection (4) of section 13 of the Public Service Pensions Act (Northern Ireland) 2014 (“the Act”). GAD has prepared this report to set out the results of our review of the 2016 funding valuation of the Local Government Pension Scheme Northern Ireland (LGPS NI). This report will be of relevance to NILGOSC and other employers, actuaries performing valuation for the fund, the LGPS NI Scheme Advisory Board (SAB), Department of Finance (DoF) and the Chartered Institute of Public Finance & Accountancy (CIPFA), as well as other LGPS NI stakeholders.

2.8 We have concluded that the 2016 actuarial valuation of LGPS NI and the resulting employer contribution rates achieve the aims set out in Section 13 in respect of compliance, consistency, solvency and long-term cost efficiency. We have therefore not recommended any remedial steps in this report.

Structure of the report

2.9 In the remaining sections in this report, we consider each of the four aims of section 13 for LGPS NI:

- > Compliance
- > Consistency
- > Solvency
- > Long term cost efficiency

2.10 The appendices to the report contain further information on the data and assumptions used for this exercise, section 13 of the Public Service Pensions Act 2014 and extracts from other relevant regulations.

2.11 This report should be read along with the LGPS England and Wales section 13 report (including the appendices to that report)⁵.

2.12 In the remainder of this introduction we consider:

⁵ <https://www.gov.uk/government/publications/local-government-pension-scheme-review-of-the-actuarial-valuations-of-funds-as-at-31-march-2016>



- > Metrics and flags we use to identify potential issues in respect of solvency and long term cost efficiency
- > Limitation of this report
- > The role of the fund actuary and other stakeholders
- > Data and assumptions used in this report
- > Engagement with stakeholders in preparing this report
- > Compliance and liability

Metrics and flags

2.13 We have looked at a range of metrics to identify potential issues in respect of solvency and long term cost efficiency. The fund's score under each measure is colour coded or flagged, where:

GREEN indicates that there are no material issues that may contribute to a recommendation for remedial action in order to ensure Solvency or Long Term Cost Efficiency

AMBER indicates a potential issue should be recognised but in isolation would not usually contribute to a recommendation for remedial action in order to ensure Solvency or Long Term Cost Efficiency

RED indicates a potentially material issue that may contribute to a recommendation for remedial action in order to ensure Solvency or Long Term Cost Efficiency

2.14 While they should not represent targets, these measures and flags help us determine whether a more detailed review is required; for example, we might have concern where multiple measures are triggered amber for the fund.

2.15 In broad terms, amber flags are advisory signals that may indicate action and/or a need for further investigation through engagement with NILGOSC and its actuary. It should be noted that these flags are intended to highlight areas where risk may be present, or further investigation is required. Where an amber flag remains following that engagement, we believe this relates to an area where an issue remains that NILGOSC and the pension board should be aware of. There is no implication that NILGOSC was previously unaware of the issue or the action taken was inappropriate.

2.16 A green flag (ie the absence of a red or amber flag) does not necessarily indicate that no risk is present and similarly the fact that we are not specifically suggesting remedial action does not mean that NILGOSC should not consider actions.

2.17 For the LGPS NI 2016 valuation:

- > In respect of Solvency, all metrics were green flagged, except
 - Non-statutory members metric was amber flagged



- Asset shock metric was green flagged because the scheme was in surplus on GAD's best estimate basis, but changes in asset values may put upward pressure on employer contribution rates and if the scheme had not been in surplus it would have been amber flagged
- > In respect of Long Term Cost Efficiency, all metrics were green flagged

Limitations

- 2.18 We recognise that the use of data and models has limitations. For instance, the data that we have from valuation submission and publicly available financial information is likely to be significantly less detailed than that available to the fund. Our risk assessment framework is designed to broadly assess scheme risks and decide on our engagement on an indicative basis.
- 2.19 Because of the nature of this exercise, the only post valuation events considered are those that may have already been taken into account in the valuation disclosure.
- 2.20 Further detail is provided in the solvency and long term cost efficiency chapters and appendices.

The role of the fund actuary and other stakeholders

- 2.21 Local valuation output depends on the local circumstances of the fund, NILGOSC's Funding Strategy Statements, and the actuary's work on the valuation.
- 2.22 It is not our role to express an opinion as to whether any concerns raised are driven by the local circumstances of a fund, or the actions of authorities, their actuary, or other stakeholders. Nothing in this report should be taken as criticism of authorities, their actuary, or other stakeholders.

Data and assumptions

- 2.23 The metrics are based on publicly available data and data provided to GAD by or on behalf of NILGOSC.
- 2.24 Further details of the data used for the purpose of this exercise can be found in Appendix A of this report.
- 2.25 To make meaningful comparison of valuation results, we have referred to results restated on two bases:
- > The standard basis established by the LGPS England and Wales SAB, as used in the LGPS England and Wales Section 13 report
 - > A market consistent best estimate basis derived by GAD based on the investment strategy for LGPS NI
- 2.26 Further details of both these bases are set out in Appendix B to this report.



- 2.27 The market consistent basis is GAD's best estimate as at 2016, based on our views of likely future returns on each asset class in the Scheme. Future asset returns are uncertain and there is a wide range of reasonable views on what future asset returns will be and therefore the best estimate discount rates should be. We have presented GAD's view above, but there are other reasonable best estimate bases that may give materially different results.
- 2.28 The use of these standard bases does not imply the bases are suitable to be used for funding purposes:
- > The LGPS England and Wales SAB standard basis is not market consistent
 - > The best estimate basis does not take into account any anticipated changes in investment strategy that may be planned/in train
 - > Statutory CIPFA guidance calls for prudence to be adopted in valuation bases
- 2.29 The local valuation and our calculations underlying this report are based on specific sets of assumptions about the future. Some of our solvency measures are stress tests but these are not intended to indicate a worst-case scenario.

Engagement with stakeholders

- 2.30 In preparing this report, we are grateful for helpful discussions with and cooperation from:
- > DfC
 - > NILGOSC
 - > NILGOSC's actuarial advisors
- 2.31 We note that this report is GAD's alone and the stakeholders above are not responsible for the content.
- 2.32 We are committed to preparing a section 13 report that makes practical recommendations to advance the aims in the legislation. We will continue to work with stakeholders to advance these aims and expect that our approach to section 13 will continue to evolve to reflect ever-changing circumstances and feedback received.

Compliance and liability

- 2.33 This work has been carried out in accordance with the applicable Technical Actuarial Standard: TAS 100 issued by the Financial Reporting Council (FRC). The FRC sets technical standards for actuarial work in the UK.
- 2.34 GAD has no liability to any person or third party for any act or omission taken, either in whole or in part, on the basis of this report. No decisions should be taken on the basis of this report alone without having received proper advice. GAD is not responsible for any such decisions taken.



- 2.35 We understand and assume that there is no regulatory authority assumed by or conferred on the Government Actuary in preparing this or any future section 13 report, and neither does the appointment to report under section 13 give the Government Actuary any statutory power to enforce actions on scheme managers (or others).



3 Compliance

KEY COMPLIANCE FINDINGS

- > THE 2016 VALUATION REPORT CONTAINED A STATEMENT OF COMPLIANCE
- > THE REPORT CONTAINED CONFIRMATION OF EACH OF THE REQUIREMENTS IN REGULATION 68
- > WE CONCLUDED THAT THE AIMS OF SECTION 13 WERE ACHIEVED UNDER THE HEADING OF COMPLIANCE

- 3.1 Section 13 requires that GAD must report on whether the actuarial valuation of the fund has been completed in accordance with the scheme regulations.
- 3.2 We found that the actuarial valuation report for Northern Ireland Local Government Officers' Pension Fund has been completed in accordance with Regulation 68, and have therefore concluded that the compliance criteria of section 13 have been achieved. We note that this is not a legal opinion.
- 3.3 Our review of compliance is focused on the actuarial valuation report produced under Regulation 68. We have not, for example, systematically reviewed the Funding Strategy Statement prepared under Regulation 64.
- 3.4 We carried out the same checks for LGPS NI as LGPS England and Wales funds. These checks are detailed in Appendix A of the appendices to the England and Wales Section 13 report⁶.
- 3.5 The comments we make in subsequent chapters on consistency, solvency and long-term cost efficiency do not imply that we believe that the valuations are not compliant with the regulations. These comments relate only to whether the valuation appears to achieve the aims of section 13.

⁶ The appendix refers to Regulation 62 of the LGPS Regulations 2013. The relevant scheme regulation for LGPS NI from the LGPS Regulations NI 2014 is Regulation 68.



4 Consistency

KEY CONSISTENCY FINDINGS

- > THERE IS ONLY ONE PENSION FUND IN LGPS NI, NORTHERN IRELAND LOCAL GOVERNMENT OFFICERS' PENSION FUND
- > THEREFORE THERE ARE NO CONSISTENCY ISSUES TO ADDRESS AS PART OF SECTION 13 REVIEW
- > THE OUTCOME OF THE RECOMMENDATIONS MADE TO ENGLAND AND WALES SAB UNDER CONSISTENCY FOR SECTION 13 MIGHT BE OF INTEREST TO NILGOSC

- 4.1 Section 13(4)(b) requires GAD to report on whether actuarial valuation has been carried out in a way which is not inconsistent with other actuarial valuations of the pension fund completed under the scheme regulations.
- 4.2 However, as there is only one fund in LGPS NI, there are no "other actuarial valuations" in respect of LGPS NI to compare with.
- 4.3 We considered consistency among the valuation reports of the 91 local authority funds for LGPS England and Wales. There were inconsistencies on the presentation of disclosures and the assumptions adopted among the funds advised by different firms of actuarial advisors. We made recommendations to the LGPS England and Wales Scheme Advisory Board to consider steps to ensure greater consistency to better facilitate comparison. LGPS NI stakeholders may wish to consider whether there are any changes that may be of interest for LGPS NI, once the outcome of that process is known.
- 4.4 In future reviews, we will consider if it will be appropriate to compare the valuation report with the previous valuation report for consistency.



5 Solvency

KEY SOLVENCY FINDINGS

- > IN OUR VIEW, LGPS NI PENSION FUND MEETS THE CONDITIONS REQUIRED TO BE ABLE TO DEMONSTRATE SOLVENCY
- > LGPS NI HAS SIGNIFICANT PROPORTION OF RETURN SEEKING ASSETS, WHICH IS TYPICAL OF MOST LGPS FUNDS. NILGOSC IS AWARE OF THE RISK AND PROVIDED EVIDENCE ON HOW IT MANAGES THIS RISK
- > NILGOSC MIGHT WANT TO CONSIDER WHETHER ANY FURTHER ACTIONS ARE NEEDED TO COMMUNICATE THIS RISK TO STAKEHOLDERS, INCLUDING EMPLOYERS.
- > LGPS NI HAS A GREATER PROPORTION OF NON-STATUTORY EMPLOYERS (EG HOUSING ASSOCIATIONS, UNIVERSITIES, COLLEGES, SCHOOLS) THAN ANY LGPS ENGLAND AND WALES FUND. NILGOSC IS ACTIVELY MANAGING THIS RISK THROUGH ITS COVENANT ASSESSMENT PROCESS. NILGOSC MAY WISH TO CONSIDER MONITORING POTENTIAL EXIT PAYMENT AMOUNTS AS PART OF THEIR PROCESS.

5.1 Under section 13(4)(c) of the Act, the Government Actuary must report on whether the rate of employer contributions to the fund is set at an appropriate level to ensure the solvency⁷ of the pension fund.

⁷ The explanatory notes to the Act state that solvency means that the rate of employer contributions should be set at "such a level as to ensure that the scheme's liabilities can be met as they arise".



Definition of Solvency

- 5.2 We do not regard that Solvency means that a pension fund should be 100% funded at all times. Rather, in line with the definition in CIPFA's Funding Strategy Statement Guidance⁸ which we adopt for the purposes of section 13, we consider that the rate of employer contributions has been set at an appropriate level to ensure solvency of the pension fund if:
- > the rate of employer contributions is set to target a funding level for the whole fund (assets divided by liabilities) of 100% over an appropriate time period and using appropriate actuarial assumptions
- and
- > 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%
- 5.3 Solvency is dependent on employers being able to pay contributions as required, knowing that these contributions may increase or decrease significantly in future. In the case of tax-raising employers, accommodating contribution variability is a political, as well as financial, consideration. We consider it is important that NILGOSC and LGPS NI employers understand the potential range of future cost, so that they can understand the affordability of potential future contribution requirements.
- 5.4 We carried out an asset liability modelling exercise as part of England and Wales Section 13 report. This might be of interest to NILGOSC to gain some insight into the potential pressures on the employer contribution rate that might need to be managed in some way.
- 5.5 NILGOSC might want to consider whether any further actions are needed to communicate the risk of employer contribution volatility to stakeholders, including employers.

Solvency measures

- 5.6 We have tested the following five metrics under solvency, similar to the England and Wales 2016 section 13 exercise. These include a series of tests in relation to emerging risks. These are stress tests in relation to what may happen if certain events occur. The results for LGPS NI are also included in the table below:

⁸ <http://www.cipfa.org/policy-and-guidance/publications/p/preparing-and-maintaining-a-funding-strategy-statement-in-the-lgps-2016-edition>



Table 5.1: 2016 Solvency measures

Consideration	Measure Used	LGPS NI results
Risks already present:		
The relative ability of the fund to meet its accrued liabilities	Funding level on England and Wales SAB standard basis: Comparison of the fund's funding level with the mean funding level for the England and Wales funds, both funding levels calculated using the England and Wales SAB standard basis, as set out in Appendix D	+11.7%
The extent to which the fund continues to be open to new members. If a fund is closed to new members or is highly mature, we will focus on the ability to meet additional cash contributions	Open fund: Whether the fund is open to new members	Yes
The proportion of scheme employers without tax raising powers or without statutory-backing	Non-statutory members: The proportion of members within the fund who are/were employed by an employer without tax raising powers or statutory backing	26.0%
Emerging risks:		
The cost risks posed by changes to the value of scheme assets (to the extent that these are not matched by changes to the scheme liabilities)	Asset shock: The change in average employer contribution rates expressed as a percentage of payroll after a 15% fall in value of return-seeking assets	Surplus (5.3%)
The impact that non-statutory employers defaulting on contributions would have on the income of sponsoring employers as a whole	Employer default: The change in average employer contribution rates as a percentage of payroll if all employers without tax raising powers or statutory backing default on their existing deficits	Surplus

5.7 Further details on the calculations underlying the numbers are given in appendix C of the England and Wales Section 13 Appendices. There are some LGPS NI specific differences which are detailed below:

- > The results on the England and Wales SAB basis were estimated by GAD. For England and Wales funds, these results were provided by the fund actuaries.
- > The data for non-statutory employees was provided by NILGOSC, further details are included in Appendix A of this report.



- > The change in average employer contribution rates for asset shock and employer default shock is expressed as a percentage of payroll for LGPS NI rather than core-spending power or financing data as was the case for English funds and Welsh funds respectively.

Background on solvency

- 5.8 The funding level on valuation basis has improved from 91% to 96% since 2013 valuation. On GAD's best estimate basis, the funding level at 2016 was 122%. This means that we expect there is a greater than 50% chance that existing assets would be sufficient to cover benefits in respect of accrued service when they fall due.
- 5.9 We have assessed risk against a range of measures. These are risks of potential contribution volatility that NILGOSC should be aware of. Managers should consider actions required to manage these risks, but accepting the risk may be a valid option. The flag does not imply that anything has gone wrong and maintaining the flag does not imply that we take issue with any decision to accept the risk. The amber flag is an indication that the risk is accepted or has not been mitigated – it is not implying that NILGOSC is unaware of the risk.
- 5.10 Funds should be aware of their solvency position, to ensure that the relevant plans are in place to be able to pay benefits when they fall due and employers are able to accommodate potential future increases in contributions.

Asset Shock

- 5.11 Asset shock considers the scenario of a sustained reduction in the value of return seeking assets. For example, this could be a market correction in which asset values do not immediately recover, and therefore cannot be absorbed by a change in assumptions. In this scenario we model the additional contributions that would be required to meet the emerging deficit (as opposed to the total contributions required following the shock – ie we are looking at where there is a risk of large changes to the contribution rate, rather than a risk of the total contribution rate exceeding some threshold).
- 5.12 A shock, which generates high additional contributions as a proportion of payroll, generates a flag as this may indicate that the fund may be less likely to be able to absorb substantial contribution increases without affecting core services.
- 5.13 Although the asset shock resulted in a reduction to the funding level of the scheme on GAD's best estimate basis, it remained in surplus post shock (the funding level was in excess of 100% after the shock). The fund is therefore green flagged on this measure. However the reduction in the funding level following the asset shock was equivalent to a 5.3% increase in employer contributions. On comparison with the England and Wales funds, the fund would have been in the most negatively affected quartile for the increase in contributions post shock. In practice we might not expect these pressures to feed directly into changes in employer contribution rates, because there are various ways in which such a cost pressure might be managed, at least in the short term.



- 5.14 We sought further information from NILGOSC about how they are managing this risk. Investment risk is included in NILGOSC's funding strategy statement. NILGOSC provided us with evidence that they undertook a review of the fund's strategic funding target and its target asset allocation in autumn 2017. NILGOSC is moving to a less risky portfolio. We understand that this is not expected to result in reduced discount rates or increased employer contributions.
- 5.15 This indicates that the fund is aware of this risk and is actively managing it. In preparing this report we have considered only the risk management processes; we have not reviewed and do not comment on the appropriateness of the current or proposed investment strategy.

Non-statutory employers

- 5.16 In the case of tax raising employers, accommodating contribution variability is a political, as well as financial, consideration. We consider it is important that NILGOSC and other employers understand the potential range of future cost, so that they can understand the affordability of potential future contribution requirements.
- 5.17 We have considered tax payer-backed employers of stronger covenant value than other employers. It is important, in this context, that NILGOSC and other employers understand the potential cost that may fall on taxpayers in the future if employers without statutory backing or tax raising powers are unable to meet their required contributions and those with such powers become responsible for the accrued costs.
- 5.18 Data for this measure was provided by NILGOSC. The measure is based on the proportion of active members who are employed by employers, which do not have tax raising powers. We have assumed that only the following employers are tax backed:
- > Council
 - > Education Authority
 - > Employers with guarantee from council
 - > Employers with departmental backing

And we have considered the following employers to be non-tax backed following discussions with NILGOSC:

- > Housing Associations
- > Universities
- > Colleges
- > Schools
- > Northern Ireland Housing Executive



- > Translink
- > Employers from other authorities without council guarantee or departmental backing

- 5.19 At 26.0%, LGPS NI has a greater proportion of non-statutory employers than any LGPS England and Wales fund. Most of these employers are public bodies which receive public funding but do not have powers to raise taxes. Although LGPS NI has the highest proportion, and is just above the threshold of 25% for an amber flag, it is not an outlier: there are a couple of England and Wales funds with a proportion of 24.5% and 22.8%.
- 5.20 If such employers exit the scheme, they are liable to pay an exit payment to cover their liabilities in the scheme (net of any associated assets). However if it is not possible to obtain all or part of the exit payment due from them, costs fall back on the other scheme employers. We understand that in 2013-16, a total of 5 exiting employers defaulted on their exit payments, leaving unpaid exit payments of £3.6 million. This figure can be compared with total employer contributions of £535 million over the same period⁹ (ie the unpaid exit payments represent about 0.7% of employer contributions received). This means that other employers are essentially insuring for the risk posed by these employers without charging any premium for it. NILGOSC acts to mitigate this risk as discussed below.
- 5.21 NILGOSC has recognised this risk in the fund's Funding Strategy Statement. To manage this risk, NILGOSC formally assesses the covenant strength of its scheme employers on a triennial basis. This exercise is completed in advance of each actuarial valuation and is used to inform the valuation and subsequent grouping of employers for contribution rate setting purposes. A five point scale is used to categorise each employer which ranges from "A - Strong" to "E - Weak".
- 5.22 Employers categorised D or E have higher funding targets. Those category D or E employers that are not already on a flight path to closure are treated on the Intermediate Funding basis. Those that are on a flight path to closure are treated on an Orphan basis. For example, the left-service discount rate used for main employer group funding target is 4.5% whereas that for an intermediate funding target and orphan body funding target is 3.5% and 2.5% respectively which leads to higher contributions than stronger employers in similar circumstances in the main group.
- 5.23 This helps to improve their funding level and reduce any balance that would be due as an exit payment, therefore reducing the impact of any potential default and a call on other employers. However there is a limit to contributions that can be charged to these employers: if contributions are too high it might trigger insolvency (or similar issues), leading to the employer exiting the fund and the need for an exit payment. We understand that the five exiting employers that defaulted on their exit payments were all classified either D or E.

⁹ LGPS NI Valuation as at 31 March 2016, Aon Hewitt, 29 March 2017, Appendix 5, p39.



- 5.24 All employers complete an annual update as part of the covenant assessment process which is reviewed for material changes. This review can lead to employers being moved to different covenant strength categories at the next valuation. Some examples of employers moving from the main group to the 'intermediate funding target' status at the 2016 valuation include Coleraine Harbour Commissioners, Linen Hall Library, Community Relations Council, Northern Ireland Hospice and Belfast Visitor & Convention Bureau. Employers in the main group typically paid contributions averaging 19% pay (with additional contributions expressed as a monetary amount); these employers paid higher rates up to 26.2% pay (also with additional contributions expressed as a monetary amount).
- 5.25 We understand that the assessment of the employer covenant strength process is part of NILGOSC's internal control system which is evaluated annually by an external firm of internal auditors, and in addition it has been subject to a specific audit.
- 5.26 We understand that at triennial valuations NILGOSC's actuary provides the exit payment that would be due from each employer (if they were to have exited on the valuation date). NILGOSC may wish to monitor these figures as part of its process for managing this risk. For example:
- > Employers with a combination of relatively weak employer covenant and a high exit payment (if they were to exit) may merit the most attention in the process of monitoring employer covenant
 - > The total exit payment for each of the five categories of employers from "A - Strong" to "E - Weak" could be used at each valuation to monitor changes in this risk over time: increases / decreases to the total value of exit payments in respect of weaker employers indicate that the value at risk is increasing / decreasing.



6 Long term cost efficiency

KEY LONG TERM COST EFFICIENCY FINDINGS

- > IN OUR VIEW, LGPS NI PENSION FUND MEETS THE CONDITIONS REQUIRED TO BE ABLE TO DEMONSTRATE LONG TERM COST EFFICIENCY
- > LGPS NI HAS GREEN FLAGS ON ALL OUR LONG TERM COST EFFICIENCY MEASURES
- > IF AT A FUTURE VALUATION IT WAS POSSIBLE FOR EMPLOYER CONTRIBUTIONS TO BE REDUCED, WE SUGGEST THAT NILGOSC CONSIDER MAINTAINING THE DEFICIT RECOVERY END POINT OR MOVING IT FORWARDS

- 6.1 Under section 13(4)(c) of the Act, the Government Actuary must report on whether the rate of employer contributions to the pension fund is set at an appropriate level to ensure the long-term cost efficiency¹⁰ of the scheme, so far as relating to the pension fund.

¹⁰ Explanatory notes to the Act state that: "Long-term cost-efficiency implies that the rate must not be set at a level that gives rise to additional costs. For example, deferring costs to the future would be likely to result in those costs being greater overall than if they were provided for at the time."



Definition of Long Term Cost Efficiency

6.2 In line with the definition in CIPFA's Funding Strategy Statement Guidance¹¹, which we adopt for the purposes of section 13, we consider that the rate of employer contributions has been set at an appropriate level to ensure long term cost efficiency if the rate of employer contributions is sufficient to make provision for the cost of current benefit accrual, with an appropriate adjustment to that rate for any surplus or deficit in the fund.

Long Term Cost Efficiency Measures

6.3 We developed a series of relative and absolute considerations to help assess whether the contributions met the aims of section 13 under Long Term Cost Efficiency, similar to the England and Wales section 13 exercise.

6.4 The table below gives details of these measures along with the results for LGPS NI:

Table 6.1: Long Term Cost Efficiency Considerations and Measures

Consideration	Measure Used	LGPS NI Result
Relative considerations:		
The implied deficit recovery period	Deficit Period: Implied deficit recovery period calculated on a standardised best estimate basis	Surplus
The investment return required to achieve full funding	Required Return: The required investment return rates to achieve full funding in 20 years' time on a standardised best estimate basis	3.0%
The pace at which the deficit is expected to be paid off	Repayment Shortfall: The difference between the actual deficit recovery contribution rate and the annual deficit recovery contributions required as a percentage of payroll to pay off the deficit in 20 years, where the deficit is calculated on a standardised best estimate basis	8.8%

¹¹ <http://www.cipfa.org/policy-and-guidance/publications/p/preparing-and-maintaining-a-funding-strategy-statement-in-the-lgps-2016-edition>



Consideration	Measure Used	LGPS NI Result
Absolute Considerations:		
The extent to which the required investment return above is less than the estimated future return being targeted by a fund's investment strategy	Return Scope: The required investment return rates as calculated in required return, compared with the fund's expected best estimate future returns assuming current asset mix maintained	2.8%
The extent to which any deficit recovery plan can be reconciled with, and can be demonstrated to be a continuation of, the previous deficit recovery plan, after allowing for actual fund experience	Deficit Reconciliation: Confirmation that the deficit period can be demonstrated to be a continuation of the previous deficit recovery plan, after allowing for actual fund experience.	Green

6.5 The calculations underlying these results are same as those for the England and Wales section 13 exercise, except to allow for LGPS NI specific differences. Further details are given in Appendix D in the appendices to the England and Wales section 13 report, with slight differences as listed below:

- > The cashflow data underlying the required return measure was obtained from the revenue accounts information provided by NILGOSC, whereas for England and Wales funds, it was based on the SF3 data.
- > The best estimate basis used in these calculations is specific to the asset allocation for the LGPS NI fund. Further details on this are given in Appendix B of this report.

Background on long term cost efficiency

6.6 Long Term Cost Efficiency relates to not deferring payments too far into the future so that they affect future generations of taxpayers disproportionately.

6.7 Following the 2016 valuation, the funding level has improved significantly from 91% to 96%. This follows a strong period of asset outperformance, but also greater levels of contributions being paid into the fund.

Deficit Reconciliation

6.8 At the 2016 valuation, employer contribution rates increased and the deficit recovery period changed from 2014-34 to 2017-37. The length of the deficit recovery period was 20 years in both cases, and the deficit recovery end point moved back from 2034 to 3037. We have no concerns about this in the context of increasing employer contribution rates.



- 6.9 We would not normally expect to see employer contribution rates decreasing (reducing the burden on current taxpayers) at the same time as the deficit recovery end point being extended further into the future (increasing the burden on future taxpayers). This is consistent with CIPFA guidance that over time and given stable market conditions, LGPS funds should aim to reduce deficit recovery periods. If at a future valuation it was possible for employer contributions to be reduced, we suggest that NILGOSC consider maintaining the deficit recovery end point (or moving it forwards), rather than moving it backwards.



Appendix A: Data provided

- A.1 Data was received from the fund actuary for NILGOSC as detailed in Appendix F of the appendices to the England and Wales section 13 report. There were some LGPS NI specific differences. These are detailed below:
- A.1.1 Results on England and Wales SAB standard basis were not provided by LGPS NI fund actuary, these were estimated by GAD.
 - A.1.2 Data in respect of the breakdown of members employed by employers with tax raising powers was received from NILGOSC.
 - A.1.3 There was no core spending data available for LGPS NI, so we did not use this information in our metrics. Instead, we based our metrics on payroll, which was provided by the fund actuary.
 - A.1.4 There were no SF3 statistics available for LGPS NI. Instead, we used information submitted to us in the revenue accounts section of the data submission as part of the data collection exercise.
 - A.1.5 The comments about missing information are specific to the funds identified in the appendix and do not apply to LGPS NI.
 - A.1.6 The primary contribution rate refers to the common contribution rate in the LGPS NI valuation report.



Appendix B: Assumptions

B.1 Each section of analysis contained in the main report is based on one of three sets of assumptions:

- > The local fund assumptions, as used in the fund's 2016 actuarial valuation
- > The LGPS England and Wales SAB standardised set of assumptions (E&W SAB standard basis)
- > A best estimate set of assumptions

B.2 Details of the LGPS NI assumptions can be found in the NILGOSC actuarial valuation report as at 31 March 2016. Details of the E&W SAB standard basis and the standardised best estimate basis can be found in the table below. Differences are highlighted.

Table B.1: E&W SAB standard basis¹² and Best Estimate basis

ASSUMPTION	E&W SAB standard basis	Best Estimate basis
METHODOLOGY	Projected Unit Methodology with 1 year control period	Projected Unit Methodology with 1 year control period
RATE OF PENSION INCREASES	2% per annum	1.90% per annum
PUBLIC SECTOR EARNINGS GROWTH	3.5% per annum	3.90% per annum
DISCOUNT RATE	5.06% per annum	5.79% per annum
PENSIONER BASELINE MORTALITY	Set locally based on Fund experience	
MORTALITY IMPROVEMENTS	Set locally based on Fund experience	
CHANGES TO STATE PENSION AGE	As legislated	
AGE RETIREMENT	Set locally based on Fund experience	
ILL HEALTH RETIREMENT RATES	Set locally based on Fund experience	
WITHDRAWAL RATES	Set locally based on Fund experience	
DEATH BEFORE RETIREMENT RATES	Set locally based on Fund experience	
PROMOTIONAL SALARY SCALES	None	Set locally based on Fund experience
COMMUTATION	E&W SAB future service cost assumption of 65% of the maximum allowable amount.	Set locally based on Fund experience
FAMILY STATISTICS	Set locally based on Fund experience	

¹² Details can be found in the England and Wales Scheme Advisory Board's Cost Management Process of 5 February 2015 at: <http://www.lgpsboard.org/images/PDF/CMBDANov2016/AI5-SABCMP2.pdf>



- B.3 The financial assumptions for the best estimate basis are based on GAD's neutral assumptions for long term inflation measures and asset returns, and the split of LGPS NI assets held as at 31 March 2016, and are therefore different from the assumptions adopted for LGPS England and Wales section 13 report.
- B.4 These neutral assumptions are not deliberately optimistic nor pessimistic and do not incorporate adjustments to reflect any desired outcome. We believe there is around a 50% chance of outcomes being better and a 50% chance of outcomes being worse than these assumptions imply.
- B.5 Future asset returns are uncertain and there is a wide range of reasonable views on what future asset returns will be and therefore the best estimate discount rate should be. We have presented GAD's house view above, but there are other reasonable best estimate bases which may give materially different results.

Table B.2: Assumed Life Expectancy¹³

	Assumed life expectancy (years)
Current pensioners	
Male aged 65	23.1
Female aged 65	25.7

¹³ This is the assumed life expectancy of current pensioners who retired on normal health, as provided by Aon



Appendix C: Section 13 of the Public Service Pensions Act (Northern Ireland) 2014¹⁴

13 Employer contributions in funded schemes

- (1) This section applies in relation to a scheme under section 1 which is a defined benefits scheme with a pension fund.
- (2) Scheme regulations must provide for the rate of employer contributions to be set at an appropriate level to ensure—
 - (a) the solvency of the pension fund, and
 - (b) the long-term cost-efficiency of the scheme, so far as relating to the pension fund.
- (3) For that purpose, scheme regulations must require actuarial valuations of the pension fund.
- (4) Where an actuarial valuation under subsection (3) has taken place, a person appointed by the responsible authority is to report on whether the following aims are achieved—
 - (a) the valuation is in accordance with the scheme regulations;
 - (b) the valuation has been carried out in a way which is not inconsistent with other valuations under subsection (3);
 - (c) the rate of employer contributions is set as specified in subsection (2).
- (5) A report under subsection (4) must be published; and a copy must be sent to the scheme manager and (if different) the responsible authority.
- (6) If a report under subsection (4) states that, in the view of the person making the report, any of the aims in that subsection has not been achieved—
 - (a) the report may recommend remedial steps;
 - (b) the scheme manager must—
 - (i) take such remedial steps as the scheme manager considers appropriate, and
 - (ii) publish details of those steps and the reasons for taking them;
 - (c) the responsible authority may—
 - (i) require the scheme manager to report on progress in taking remedial steps;
 - (ii) direct the scheme manager to take such remedial steps as the responsible authority considers appropriate.

¹⁴ <https://www.legislation.gov.uk/nia/2014/2/section/13>



- (7) The person appointed under subsection (4) must, in the view of the responsible authority, be appropriately qualified and must not be—
- (a) an employee of the responsible authority;
 - (b) the scheme manager;
 - (c) a scheme member; or
 - (d) an employee of the Department of Finance and Personnel.



Appendix D: Extracts from other relevant regulations

Regulations 64 and 68 of 'The Local Government Pension Scheme Regulations (Northern Ireland) 2014'¹⁵

Funding strategy statement

- 64.– (1) The Committee shall, after consultation with such persons as it considers appropriate, prepare, maintain and publish a written statement setting out its funding strategy.
- (2) The statement shall be published no later than 31st March 2015.
- (3) The Committee shall keep the statement under review and, after consultation with such persons as it considers appropriate, make such revisions as are appropriate following a material change in its policy set out in the statement and, if revisions are made publish the statement as revised.
- (4) In preparing, maintaining and reviewing the statement, the Committee shall have regard to—
- (a) the guidance set out in the document published in October 2012 by CIPFA, the Chartered Institute of Public Finance and Accountancy and called "Preparing and Maintaining a Funding Strategy Statement in the Local Government Pension Scheme 2012" ; and
 - (b) the statement of investment principles published by the Committee under regulation 10 (statement of investment principles) of the 2000 Regulations.

Actuarial valuations and certificates

- 68.– (1) The Committee shall obtain—
- (a) an actuarial valuation of the assets and liabilities of the pension fund, as at 31st March 2016 and on 31st March in every third year afterwards;
 - (b) a report by an actuary in respect of the valuation; and
 - (c) a rates and adjustments certificate prepared by an actuary.
- (2) Each of those documents shall be obtained before the first anniversary of the date ("the valuation date") as at which the valuation is made or such later date as the Department may agree.
- (3) A report under paragraph (1)(b) shall contain a statement of the demographic assumptions used in making the valuation and the statement shall show how the assumptions relate to the events which have actually occurred in relation to members of the Scheme since the last valuation.

¹⁵ <https://www.legislation.gov.uk/nisr/2014/188/contents/made>



- (4) A rates and adjustments certificate is a certificate specifying—
- (a) the common rate of employers' contribution;
 - (b) any individual adjustments; and
 - (c) any amount calculated in accordance with paragraph (8),
- for each year of the period of three years beginning with 1st April in the year following that in which the valuation date falls.
- (5) The common rate of employers' contribution is the amount, if any, which in the actuary's opinion, should be paid to the pension fund so as to secure the fund's solvency by all contributing bodies whose employees contribute to it expressed as a percentage of the pay of their employees who are active members, or for any other employing authority or former employing authority which does not employ active members but is liable to contribute to the fund under regulation 70(12) and (13) (special circumstances where revised actuarial valuations and certificates shall be obtained) is such amount as is payable under regulation 70(13).
- (6) The actuary shall have regard to—
- (a) the existing and prospective liabilities arising from circumstances common to all those bodies;
 - (b) the desirability of maintaining as nearly constant a common rate of employers' contribution as possible;
 - (c) the current version of the Committee's funding strategy statement mentioned in regulation 64 (funding strategy statement); and
 - (d) the desirability of securing long term cost efficiency of the pension fund.
- (7) An individual adjustment is any percentage or amount by which, in the actuary's opinion, contributions at the common rate of employer's contribution should, in the case of—
- (i) a particular contributing body;
 - (ii) a particular guarantor; or
 - (iii) both employing authority and inheriting body if agreed under regulation 71 (apportionment),
- be increased or reduced by reason of any circumstances peculiar to that contributing body, guarantor or both of them and, where necessary, reflects inherited liabilities being attributable or no longer attributable.
- (8) Where inherited liabilities are attributable to a guarantor or any other person which is not an employing authority, at the direction of the Committee, the actuary shall calculate such amount which in the actuary's opinion such a guarantor or other person that is not an employing authority should pay by reason of its assumption of responsibility for these inherited liabilities.
- (9) A rates and adjustments certificate shall contain a statement of the assumptions on which the certificate is given as respects—



- (a) the number of members who will become entitled to payment of pensions under the provisions of the Scheme; and
 - (b) the amount of the liabilities arising in respect of such members, during the period covered by the certificate.
- (10) The Committee shall provide the actuary preparing a valuation or a rates and adjustments certificate with the consolidated revenue account of the pension fund and such other information as the actuary requests.