CLWYD PENSION FUND COMMITTEE

Date of Meeting	Tuesday, 23rd March 2021
Report Subject	Funding Strategy Statement – Policy Updates
Report Author	Head of Clwyd Pension Fund

EXECUTIVE SUMMARY

Regulations have come into force which provide more flexibility in relation to employer exit payments when an employer leaves the Fund and also the ability to review contributions between valuations in certain circumstances. To adopt this flexibility, Funds are required to set out their policy in their Funding Strategy Statement (FSS). Statutory guidance from MHCLG and a guide from the Scheme Advisory Board were published on 2 March 2021 and the principles in these documents have been taken into account when producing the draft policies.

A summary of the new policy areas are as follows:

- **Employer exit payments** – An exit payment can be recovered over an agreed period as opposed to being collected immediately or an employer can defer payment of the debt and enter into a Deferred Debt Arrangement (DDA) allowing the employer to remain in the Fund with no contributing members.
- **Reviewing employer contributions** - The new Regulations also permit contribution rates to be adjusted between valuations in certain circumstances.

For the Clwyd Pension Fund, we would expect these policies would be used infrequently given the type of employers and their strength of covenant. In particular, there are very few employers who can exit the Fund.

Following advice from the Fund Actuary, the proposed policies are attached as Appendix 1 (exit payments) and 2 (review of contributions) for agreement by the Committee. As required by the Regulations and guidance, a consultation with employers will then commence.

The policies will be implemented to, as far as possible, ensure employers meet their financial obligations to the Fund in terms of contributions on an ongoing and exit basis.

RECOMMENDATIONS	
1	The Committee approves the draft policies for inclusion in the FSS and consultation with employers.
2	The Committee delegate any final minor changes, following consultation, to be made by the Head of Clwyd Pension Fund and Deputy Head of Clwyd Pension Fund, with any more substantive changes being brought back to Committee for consideration.
3	The Committee agree to the updates to the Delegation of Functions which is attached at Appendix 3.

REPORT DETAILS

1.00	Funding Strategy Statement – Policy Updates
1.01	**Background and proposed governance of new arrangements** A number of regulatory changes have come into force (LGPS (Amendment No.2) Regulations 2020). These allow for more flexibilities in relation to employer exit payments when leaving the Fund via recovery of the exit payments over a period of time or allowing employers to remain in the Fund with no active members via a Deferred Debt Agreement (DDA). The Regulations also allow for employer contribution reviews between actuarial valuations in certain circumstances.
1.02	The Fund is required to include policies within its Funding Strategy Statement (FSS) setting out how the flexibilities will apply in practice to employers. The Fund will therefore update its policies to incorporate the new Regulations. These policies provide flexibilities to manage employer risk and allow the Fund to do that in a managed way.
1.03	To assist with drafting the policies and applying the Regulations, the Scheme Advisory Board (SAB) has produced a practical guide for Funds and the MHCLG has produced statutory guidance on the amendments to the FSS. These documents were published on 2 March 2021 and the principles have been taken into account when drafting the policies, following advice from the Fund Actuary.
1.04	As required by the Regulations and guidance and once the draft policies have been finalised, a short consultation with Fund employers will take place, with employer views being invited on the changes. It will also be shared with the Fund's Pension Board. Assuming any changes following this consultation is minor, the Committee are asked to delegate the finalising of the FSS to the Head of Clwyd Pension Fund Manager and Deputy Head of Clwyd Pension Fund. If there are more substantive changes then it will be brought back to Committee for consideration.
1.05	In relation to the ongoing management of these new policies, it is proposed that any initial decisions on how to treat employers are dealt with by officers of the Fund using delegated authority. Officers are already

	carrying out the management of employer exit payments through the Fund's delegated functions, and so this would be extending that authority to: • allow spreading of an employer exit payment or entering a Deferred Debt Arrangement (under the Flexibility for Exit Payments and Deferred Debt Agreements Policy) • agree a change in employer contribution outside of the formal actuarial valuation process (under the Review of Employer Contributions Between Valuations Policy) However the guidance also advises funds to agree and consult on an appeals process. As initial decisions are to be made by officers, the intention is for any appeal to be the responsibility of the Pension Fund Committee as part of their overall responsibilities in ensuring appropriate funding plans are in place for all employers in the Fund, and working with the actuary in determining the appropriate level of employer contributions for each employer. Information on the appeals process will be included in consultation with employers. Further information regarding the changes made to the policies is set out below.
1.06	**Exit Payments Flexibility** The default position for exit payments is that they are paid in full at the point of exit and this will continue under the new policy. The previous regulations generally required the exit debt to be paid in full on exit. This restricted the ability of employers to leave the Fund in an ordered and affordable manner and put the Fund (and therefore the taxpayer) at higher risk of unrecoverable debts. This is especially the case for those employers in a weak financial situation. As a consequence, employers tended to remain in the Fund building up further, often unaffordable, liabilities. The Regulations provide greater flexibility to manage this debt in conjunction with the employer and allow the employer to limit the further accrual of liabilities.
1.07	The Regulations permit LGPS funds to develop policies that provide alternative options to employers when the last active member leaves the employer (subject to a covenant assessment and consideration of security): • **Spreading payments** - Allow the Fund and the employer to enter into agreement which instead spreads the payment of the final exit debt calculated by the Actuary over an agreed period of time (the amounts and frequency of the payments in the payment plan will be agreed at the outset along with any early payment terms), or • **Deferred Debt Arrangement (DDA)** - The employer may enter into a DDA with a scheme employer. This allows the employer to defer its obligation to make an exit payment and continue to make ‘deficit’ (secondary rate) contributions to the Fund. Contribution requirements will continue to be reviewed as part of each actuarial valuation under this option, which is essentially an employer continuing ongoing participation, but with no contributing members. The Fund or employer can terminate the DDA and settle a revised (potentially more affordable) exit debt.

1.08	The Fund can only enter into one of the above arrangements if the FSS includes a policy setting out how the employer will be treated consistently. The Fund are also required to consult with the exiting employer, following advice from the Fund Actuary as well as any other specialists as appropriate as part of the process.
1.09	There are key draft policy decision points for consideration: • Spreading of exit payments or a DDA will only be entered into if the termination debt is unaffordable and; • Where the deficit is spread, the maximum spreading period is 5 years, except in exceptional circumstances. • A requirement for employers to provide ongoing covenant information and enter into a notifiable events framework. For the Clwyd Pension Fund, we would expect these policies would be used infrequently given the type of employers and their strength of covenant. In particular, there are very few employers are able to exit the Fund at this stage (e.g. Councils, Town Councils, further & higher education bodies are all required to remain in the Fund under the Regulations).
1.10	Appendix 1 sets out the draft policies for these flexibilities for the Committee to consider. The policies have been designed to strengthen the Fund's ability to manage employer liabilities, ensuring there is no detriment to the solvency of the Fund. Historically the CPF has had very few employers exiting the Fund but it is important to have a policy in place in the event this changes. In particular in relation to the new DDA option which could be in the interest of both the employer and Fund in terms of protecting taxpayers.
1.11	**Reviewing Contributions Between Triennial Valuations** The Regulations also permit contribution rates to be adjusted between valuations. Previously the contribution rates set out in the valuation report would stay in place until the next valuation except in limited circumstances or where an employer exits the Fund. These Regulations allow changes to contributions to be made before the next valuation if they meet the criteria.
1.12	Such a revision to contribution rates is only permitted if the Fund's policy is set out in the FSS and one of the following apply: • it appears likely to the administering authority that the amount of the liabilities arising or likely to arise has changed significantly since the last valuation • it appears likely to the administering authority that there has been a significant change in the ability of the Scheme employer or employers to meet the obligations of employers in the Scheme; or • a Scheme employer or employers have requested a review of Scheme employer contributions and have undertaken to meet the costs of that review (and point a) or b) also applies).
1.13	There are key draft policy decision points for consideration:

	• We have set the maximum number of requests to review contributions between actuarial valuation dates to two. • A contribution review due to a change in membership profile would not be undertaken in the 6 months leading up to the commencement of the next valuation Rates and Adjustments Certificate. • In addition, a review will only be considered if the change in liabilities is expected to be more than 5% of the total liabilities.
1.14	Appendix 2 sets out the draft policy for the Committee to consider. The policy ensures that any contribution changes will only be due to significant liability or covenant changes which would create additional risk to the Fund or employer.

2.00	**RESOURCE IMPLICATIONS**
2.01	The new policies are likely to mean increased monitoring of employers (covenant and funding) and also greater resource requirements where employers seek to enter into a Deferred Debt Agreement, which will result in increased costs (for example, through actuarial or other fees). Where employers request under either option, the costs will be met by the employer in full. In the case of a Deferred Debt Agreement, all costs would be passed onto the employer.

3.00	**CONSULTATIONS REQUIRED / CARRIED OUT**
3.01	A consultation with employers and the Pension Board will take place following agreement by Committee.

4.00	**RISK MANAGEMENT**
4.01	This report addresses some of the risks identified in the Fund's Risk Register. Specifically, this covers the following (either in whole or in part): • Governance risk: G2 • Funding and Investment risks: F1 - F6
4.02	The funding strategy (along with the investment strategy) is a key determinant of the overall financial risk levels in the CPF. The FSS is a crucial document setting out the overall governance and controls in place to manage these risks on a whole Fund and individual employer level.

5.00	**APPENDICES**
5.01	Appendix 1 – Exit Payments Policy Appendix 2 – Review of Contributions Policy Appendix 3 - Delegation of Functions to Officers and Members by Pension Fund Committee

6.00	LIST OF ACCESSIBLE BACKGROUND DOCUMENTS
6.01	1. Current FSS. 2. Committee reports on the funding strategy statements from February 2020. 3. MHCLG Statutory Guidance 4. SAB Guidance **Contact Officer:** Philip Latham, Head of Clwyd Pension Fund **Telephone:** 01352 702264 **E-mail:** philip.latham@flintshire.gov.uk

7.00	GLOSSARY OF TERMS
7.01	(a) **CPF – Clwyd Pension Fund** – The Pension Fund managed by Flintshire County Council for local authority employees in the region and employees of other employers with links to local government in the region (b) **Administering authority or scheme manager** – Flintshire County Council is the administering authority and scheme manager for the Clwyd Pension Fund, which means it is responsible for the management and stewardship of the Fund. (c) **Deferred Debt Agreement (DDA)** – A written agreement between the Administering Authority and an exiting Fund employer for that employer to defer their obligation to make an exit payment and continue to make contributions at the assessed Secondary rate until the termination of the DDA. (d) **Deferred Employer** – An employer that has entered into a DDA with the Fund. (e) **PFC – Clwyd Pension Fund Committee** - the Flintshire County Council committee responsible for the majority of decisions relating to the management of the Clwyd Pension Fund (f) **LPB or PB – Local Pension Board or Pension Board** – each LGPS Fund has an LPB. Their purpose is to assist the administering authority in ensuring compliance with the scheme regulations, TPR requirements and efficient and effective governance and administration of the Fund. (g) **LGPS – Local Government Pension Scheme** – the national scheme, which Clwyd Pension Fund is part of (h) **Funding Strategy Statement (FSS)** – the main document that outlines how we will manage employers contributions to the Fund (i) **Triennial Actuarial Valuation** - The formal valuation assessment of

	the Fund detailing the solvency position and determine the contribution rates payable by the employers to fund the cost of benefits and make good any existing shortfalls as set out in the separate Funding Strategy Statement. (j) **Actuary -** A professional advisor, specialising in financial risk, who is appointed by pension Funds to provide advice on financial related matters. In the LGPS, one of the Actuary's primary responsibilities is the setting of contribution rates payable by all participating employers as part of the actuarial valuation exercise. (k) **CPI –** Acronym standing for "Consumer Prices Index". CPI is a measure of inflation with a basket of goods that is assessed on an annual basis. The reference goods and services differ from those of RPI. These goods are expected to provide lower, less volatile inflation increases. Pension increases in the LGPS are linked to the annual change in CPI.