



**2017**  
to 2020

# FUNDING STRATEGY STATEMENT

# Funding strategy statement

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## 1. Introduction

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This is the Funding Strategy Statement (FSS) of the Greater Manchester Pension Fund (GMPF), which is administered by Tameside MBC (*the Administering Authority*).

It has been prepared by the Administering Authority in collaboration with the GMPF Actuary, Hymans Robertson LLP, and after consultation with GMPF's employers and investment advisors. It is effective from 1 April 2017.

### 1.1 Regulatory framework

Members' accrued benefits are guaranteed by statute and defined by the LGPS Regulations. Members' contributions are fixed in the Regulations at a level which covers only part of the cost of accruing benefits. Employers currently pay the balance of the cost of delivering the benefits to members. The FSS focuses on how employer liabilities are measured, the pace at which these liabilities are funded and, insofar as is practical, the measures to ensure that employers or pools of employers pay for their own liabilities.

The FSS forms part of a framework which includes:

- The Local Government Pension Scheme Regulations 2013 and other LGPS Regulations;
- The Rates and Adjustments Certificate, which can be found appended to GMPF's triennial Actuarial Valuation report;
- Actuarial factors for valuing early retirement costs and the cost of buying extra service;
- GMPF's policy on admissions; and
- The Investment Strategy Statement (formerly the Statement of Investment Principles).

Operating within this framework, the Actuary carries out triennial valuations to set employers' contributions and provides recommendations to the Administering Authority when other funding decisions are required, for example when employers join or leave GMPF. The FSS applies to all employers participating in GMPF.

The key requirements relating to the FSS are that:

- After consultation with all relevant interested parties, the administering authority will prepare and publish its funding strategy.
- In preparing the FSS, the administering authority must have regard to:
  - FSS guidance produced by CIPFA in 2004, 2012 and 2016.
  - Its Investment Strategy Statement (formerly Statement of Investment Principles).
- The FSS must be revised and published whenever there is a material change in either the policy on the matters set out in the FSS, or the Investment Strategy Statement.
- The revised FSS should be completed and approved by the pensions committee prior to the completion of each valuation.
- The actuary must have regard to the FSS as part of the fund valuation process.

### 1.2 Reviews of FSS

The FSS is reviewed in detail at least every three years in line with triennial valuations being carried out, with the next full review due to be completed by 31 March 2020.

The FSS is a summary of GMPF's approach to funding liabilities. It is not an exhaustive statement of policy on all issues. If you have any queries please contact the GMPF Employers team in the first instance at [employersupport@gmpf.org.uk](mailto:employersupport@gmpf.org.uk)

## 2. Purpose

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### 2.1 Purpose of FSS

The statutory requirement to have an FSS was introduced in 2004. The then Office of the Deputy Prime Minister (ODPM) [now the Ministry of Housing, Communities and Local Government (MHCLG)] 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 and reflect the different characteristics of different employers in determining contribution rates;
- To support the regulatory framework to maintain as nearly constant employer contribution rates as possible and to set contributions so as to ensure the solvency and long-term cost efficiency of GMPF are met; and
- To take a prudent longer-term view of funding those liabilities.

These objectives are desirable individually, but may be mutually conflicting.

This statement sets out how the Administering Authority has balanced the conflicting aims of affordability of contributions, transparency of processes, stability of employers' contributions, and prudence in the approach to funding the liabilities across the range of employers participating in GMPF.

### 2.2 Purpose of GMPF

GMPF is a vehicle by which scheme benefits are delivered. GMPF:

- Receives and invests contributions, transfer payments and investment income;
- Pays scheme benefits, transfer values and administration costs.

One of the objectives of a funded scheme is to reduce the variability of pension costs over time for employers compared with an unfunded (pay-as-you-go) alternative.

The roles and responsibilities of the key parties involved in the management of the LGPS are summarised in the Annex.

### 2.3 Aims of the Funding Policy

The objectives of GMPF's funding policy include the following:

- To ensure the long term solvency of GMPF as a whole and the solvency of each of the notional sub-funds allocated to individual employers;
- To ensure that sufficient funds are available to meet all benefits as they fall due for payment;
- To ensure that employers are aware of the risks and potential returns of the investment strategy;
- To help employers recognise and manage pension liabilities as they accrue, with consideration as to the effect on the operation of their business where the Administering Authority considers this to be appropriate;
- To try to maintain stability of employer contributions;
- To use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer ceasing participation or defaulting on its pension obligations;
- To address the different characteristics of the disparate employers or groups of employers to the extent that this is practical and cost-effective; and
- To maintain the affordability of GMPF to employers as far as is reasonable over the longer term.

## 3. Target Funding Levels & Calculation of Contribution Rates

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### 3.1 Target funding levels

GMPF's funding target for most ongoing employers is a *funding level* of 100%, calculated using the Actuary's ongoing funding basis (see section 3.2 below). The funding level is the ratio of the market value of assets compared to the present value of the expected cost of meeting the accrued benefits.

### 3.2 Ongoing funding basis

#### 3.2.1 Demographic assumptions

The demographic assumptions are intended to be best estimates of future outcomes within GMPF as advised by the Actuary, based on past experience of GMPF and other pension funds. It is acknowledged that future life expectancy and, in particular, the allowance for future improvements in longevity, is uncertain. Employers should be aware that their contributions are likely to increase in future if longevity exceeds the funding assumptions.

The approach taken is considered reasonable in light of the long term nature of GMPF and the statutory guarantee underpinning members' benefits. The demographic assumptions vary by type of member and so reflect the different member profiles of employers.

#### 3.2.2 Financial assumptions

The key financial assumption is the anticipated return on GMPF's investments. The investment return assumption makes allowance for anticipated returns in excess of UK Government Bonds ('gilts') from growth-seeking assets such as equities. There is, however, no guarantee that growth-seeking assets will out-perform gilts. The risk of under-performance 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 long-term nature of the liabilities, a long term view of prospective returns from growth-seeking assets is taken. For the 2016 valuation, the assumption is that GMPF's investments will deliver an average additional return of 2.0% a year in excess of the return available from investing in long-dated UK gilts at the time of the valuation.

The same investment return assumptions are adopted for the majority of employers. The anticipated future return on investments may vary between employers who follow different investment strategies. In general, only variations which reduce the anticipated returns compared to the position of the majority of employers are allowed.

Pensions in payment, deferment and the pensions of active members accrued since 1 April 2014 increase in line with the Consumer Price Index ('CPI'). The assumption for future increases in CPI is set with reference to market estimates for increases in the Retail Prices Index ('RPI'), less 1% per annum to reflect the differences in the calculation of the two measures of inflation.

Following the introduction of the 2014 Scheme, salary growth has become a less material assumption. At the 2016 valuation, long-term salary growth is assumed to be equal to the future increase in RPI less 0.25% per annum.

There are some employer-specific short-term salary growth assumptions, reflecting known Government policy on public sector pay awards.

### 3.3 Funding targets for non-typical employers

For admission agreements that have no guarantor and are closed to new entrants, liabilities may be valued on a more prudent basis (i.e. using a discount rate that has a lower allowance for potential investment outperformance relative to UK Government bonds). The target in setting contributions for any employer in these circumstances is to achieve full funding on an appropriate basis by the time the agreement terminates or the last active member leaves in order to protect other GMPF employers. This policy will increase regular contributions and reduce, but not entirely eliminate, the possibility of a final deficit payment being required when a cessation valuation is carried out. *Please refer to Section 4 for the treatment of departing employers.*



GMPF may also adopt the above approach in respect of admission bodies with no guarantor and where the strength of covenant is considered to be weak but there is no immediate expectation that the admission agreement will cease. The Actuary agrees the financial and demographic assumptions to be used for each such employer with the Administering Authority.

### 3.4 Asset Share Calculations for Individual Employers

The Administering Authority does not formally account for each employer's assets separately. However, with effect from 31 March 2013, GMPF has operated a system of 'unitisation' where GMPF's assets are apportioned between employers on a monthly basis using contribution and benefit expenditure figures for each employer. This process also adjusts for transfers of assets and liabilities between employers participating in GMPF. The methodology adopted means that there will still 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 GMPF. However, this is greatly reduced compared to the *analysis of surplus* method that was used previously. As part of the valuation process, the Administering Authority's internal audit function has provided assurance on the operation of the unitisation system.

### 3.5 Derivation of Employer Contributions

Employer contributions are normally made up of two elements:

- the estimated cost of future benefits being accrued, referred to as the *future service rate*; plus
- an adjustment for the funding position of accrued benefits at the valuation date relative to GMPF's target funding level for that employer (*past service adjustment*). If there is a surplus of assets there may be a contribution reduction. However, if there is a deficit then additional contributions may be required. Any surplus or deficit contributions will be spread over an appropriate period.

The introduction of the LGPS Regulations 2013 has required contributions to be expressed in a prescribed manner, although the principles behind setting contribution rates are largely similar to before. Under the Regulations the Actuary is required to prepare a **rates and adjustment certificate** specifying:

- the primary rate of the employer's contribution; and
- the secondary rate of the employer's contribution,

for each year of the period of three years beginning with the 1st April in the year following that in which the valuation date falls (i.e. 1 April 2017 to 31 March 2020 in the case of the 2016 actuarial valuation).

The primary rate of an employer's contribution is equivalent to a future service rate. The primary rate is calculated separately for all employers participating in GMPF. This is expressed as a percentage of the pay of their employees who are active members of GMPF.

The secondary rate of an employer's contributions is any percentage or amount by which, in the Actuary's opinion, contributions at the primary rate should be increased or reduced by reason of any circumstances specific to that employer, for example any past service adjustment. The sorts of specific factors which are considered are discussed in Section 3.6.

It is the adjusted contribution rate which employers are actually required to pay. In effect, separate future service rates are calculated for each employer, and together with individual past service adjustments reflecting employer-specific spreading and phasing periods, these constitute the *adjusted contribution rate*.

In calculating this adjusted rate the actuary must have regard to -

- the existing and prospective liabilities arising from circumstances common to all those employers;
- the desirability of maintaining as nearly constant a common rate as possible;
- the current version of the administering authority's funding strategy statement; and
- the requirement to secure the solvency of the pension fund and long term cost efficiency.

It is noted that securing solvency and long term cost efficiency is a regulatory requirement whereas a constant contribution rate remains only a desirable outcome.

For some employers it may be agreed by all relevant parties to pool contributions (see section 3.9.5.)

A breakdown of each employer's contribution rates following the 2013 valuation for the financial years 2014/15, 2015/16 and 2016/17 can be found in the 31 March 2013 Actuarial Valuation report (finalised in 2014). It also identifies which employers' contribution rates have been pooled with others.

### 3.6 Risk-based Contribution Rates

Recent actuarial valuations of GMPF involved calculating contribution rates using a *deterministic* approach. It was assumed that the assumptions made at the valuation would be borne out in practice.

The disadvantage of a deterministic approach is that it does not allow GMPF, the Actuary or the employers to assess the risk associated with the proposed contribution rate. Risk in this context means the likelihood that the employer will not achieve their funding target over an appropriate time period with regard to the characteristics of the employer.

At this valuation, the GMPF Actuary is adopting a *risk-based* approach which allows for thousands of possible future economic scenarios when assessing the likelihood of contributions being sufficient to meet both the accrued and future liabilities over a given time horizon for each employer.

Setting contribution rates using a risk-based approach requires GMPF and the Actuary to consider for each employer:

- The employer's funding target (see sections 3.1-3.3 above)
- How long the employer has to reach the funding target (the *time horizon* – see Section 3.9.2 below)
- An appropriate likelihood of meeting the funding target within the time horizon (*likelihood of success*) e.g. 2/3rds or 75%.

Setting an appropriate likelihood for each employer requires an analysis of the risk posed to GMPF. Factors considered include:

- Liability profile including funding level, net cashflow (i.e. contributions received less benefits paid) and whether new members are being admitted;
- Security provided to GMPF in the form of a guarantee or an additional asset;
- The sector in which the employer operates, which may influence an employer's ability to make good any deficit which may arise in future.

More detail on the calculation of contribution rates is provided in the Actuary's report on the valuation.

Contribution rates will include expenses of administration to the extent that they are borne by GMPF.

### 3.7 Presentation of Employer Contribution Rates

Contribution rates are expressed as a % of pensionable salary for most employers. The Administering Authority may choose to specify that part of the contributions are payable as periodic lump sum cash amounts. This approach is generally applied for employers where the workforce/payroll is expected to decline in order to ensure sufficient contributions are made towards repaying any deficit.

Employers' contributions are expressed as minima, with employers able to pay additional contributions should they wish to do so. In addition, some employers may be permitted to pay contributions in advance of the date on which they would otherwise be due. Employers should discuss with the Administering Authority before electing to make one-off capital payments.

### 3.8 Allowance for early retirements

Many employers and employer pools have *early retirement allowances* built into their employer contribution rate as early retirements give rise to expected additional cost. Initially these allowances are used to fund any such costs. Costs in excess of the aggregate of the allowances are generally required to be met by separate lump sum employer contributions. Any unspent allowances are added to the employer's sub-fund at the next actuarial valuation.

Some employers have an allowance for ill health early retirements but do not have any allowance for non ill health early retirements built into their contribution rates. For these employers the costs of all non ill health early retirements are met by separate lump sum employer contributions.

Employers are able to take out an insurance policy from a third-party to protect against the cost of ill health early retirements. However, as the insurance policy is a contract between the employer and insurer, any allowance for ill health early retirements will still be included in the employer's contribution rate.

## 3.9 Solvency and Long-Term Cost Efficiency

### 3.9.1 Solvency issues & target funding levels

Under Section 13(4)(c) of the Public Service Pensions Act 2013, The Government Actuary's Department ('GAD') (as the person appointed by the responsible authority) must, following an actuarial valuation, report on whether the rate of employer contributions to the pension fund is set at an appropriate level to ensure the solvency of the pension fund and long term cost efficiency. The definitions of these terms in the CIPFA guidance are provided in Section 6.

In developing the funding strategy, and in particular, the level of solvency being targeted for each employer, the Administering Authority has had regard to the potential outcomes of the subsequent review under Section 13(4)(c) and has considered the implications for its Key Performance Indicators as determined by the Scheme Advisory Board in England and Wales.

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 GMPF. With this in mind, there are a number of prudential strategies that the Administering Authority may deploy in order to maintain employer contribution rates at as nearly a constant rate as possible. These include -

- Use of extended time horizons; [3.9.2]
- Phasing in of contribution increases / decreases; [3.9.3 – 3.9.4]
- The pooling of contributions amongst employers with similar characteristics and/or a community of interest [3.9.5]

In addition to these strategies for improving the stability of employer contributions, the Administering Authority may, at its absolute discretion, permit greater *flexibility* around the employer's contributions provided that the employer has provided additional *security* to the satisfaction of the Administering Authority. Such greater flexibility may include setting contribution rates assuming a reduced likelihood of meeting the target funding position and/or an extended time horizon/deficit recovery period, or permission to join a pool with another body (e.g. a relevant and agreeable Local Authority). Additional security may include, but is not limited to, provision of a suitable financial bond, a legally-binding guarantee from an appropriate third party, or security over an employer owned asset of sufficient value.

The degree of greater flexibility extended to a particular employer is likely to 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;
- Whether the admission agreement is likely to be open or closed to new entrants.

After including investment income, GMPF currently has positive net cash flow. Therefore, GMPF can take a medium to long term view on determining employer contribution rates to meet future liabilities through operating an investment strategy that reflects this long term view. This allows short term investment markets volatility to be managed in order to reduce volatility in employer contribution rates.



### 3.9.2 Appropriate Time Horizons

Following discussion with the Administering Authority, the actuary adopts specific time horizons for employers to achieve their funding target when calculating their contributions.

The time horizon starts at the commencement of the revised contribution rate (1 April 2017 for the 2016 valuation). For employers that continue to admit new entrants, the Administering Authority would normally expect the same time horizon to be used at successive triennial valuations, but would reserve the right to propose alternative periods, for example to improve the stability of contributions.

The Administering Authority normally targets an employer's sub-fund within GMPF to be fully funded over a period not exceeding 20 years. However, these are subject to the maximum lengths set out in the table.

Type of employer	<i>Maximum</i> length of time horizon
Employers listed under Part 1 or Part 2 of Schedule 2 to the 2013 LGPS Regulations (generally Statutory Bodies with tax raising powers and other Government 'supported' employers)	A period not exceeding 20 years
Community Admission Bodies with funding guarantees, subject to the approval of the guarantor and the agreement of the Administering Authority	A period not exceeding 20 years
Transferee (Best Value) Admission Bodies	The period from the start of the revised contributions to the end of the employer's contract or as otherwise agreed with the parent Local Authority letting the contract
All other types of employer	A period equivalent to the expected future working lifetime of the remaining scheme members or such other period approved by the Administering Authority.

This *maximum* period is used in calculating each employer's minimum contributions. Employers may opt to pay higher regular contributions than these minimum rates.

### 3.9.3 Phasing in of Contribution Rises and Reductions

The Administering Authority may elect to phase in any material changes to contribution rates. Phasing in periods will be influenced by the perceived credit worthiness of the employer.

### 3.9.4 The Effect of Opting for Longer Spreading or Phasing-In

Employers in deficit that are permitted and elect to use a longer time horizon or to phase-in contribution changes will be assumed to incur a greater loss of investment returns due to the fact that their assets will build up at a slower rate by opting to defer repayment. Thus, deferring paying contributions is expected to lead to higher contributions in the long-term (depending on the actual financial and demographic performance of GMPF relative to valuation assumptions).

### 3.9.5 Pooled contributions

The Administering Authority allows employers of similar types to pool their contributions as a way of sharing experience and smoothing out the impact of experience on contribution rates.

Each of the ten Greater Manchester local authorities are the major employers in pools containing certain related employers. Upon a new employer joining GMPF, consideration is given by the Administering Authority and the relevant local authority on the appropriateness of joining a local authority pool.

Following GMPF becoming the sole Administering Authority for the Probation Service with effect from 1 June 2014, GMPF has also created a pool for the Community Rehabilitation Companies ('CRCs') and their sub-contractors.

In addition, separate pools are operated for some academy schools, colleges, town and parish councils and for smaller admission bodies. No new employers have been admitted to these pools for some time.

Those employers that have been pooled are identified in the Rates and Adjustment Certificate which is detailed in the 31 March 2016 Actuarial Valuation report (finalised in 2017).

Employers who do not wish to continue with current/historic pooling arrangements are requested to discuss the issue with the Administering Authority.

## 4. Other Aspects of Funding Strategy

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### 4.1 Background

In addition to the collection of regular contributions from employers, GMPF will seek additional contributions from employers in certain circumstances in order to maintain the solvency of GMPF and protect the interests of other employers.

### 4.2 Exiting employers

#### 4.2.1 Admission Bodies

An admission body is assumed to become an *exiting employer* under Regulation 64 of the 2013 LGPS Regulations on the termination of its admission agreement.

Admission agreements for transferee contractors are assumed to terminate at the end of the contract unless otherwise agreed by the relevant local authority and Administering Authority.

Admission agreements for other employers are assumed to terminate for any of the following reasons unless otherwise agreed by the relevant local authority and Administering Authority:

- Last active member ceasing active membership in GMPF;
- 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 Administering Authority;
- A failure by the admission body to pay any sums due to GMPF within the period required by the Administering Authority; or
- The failure by the admission body to renew or adjust the level of the bond or indemnity or to confirm appropriate alternative guarantor as required by GMPF.

In addition either party can voluntarily terminate the admission agreement by giving the appropriate period of notice as set out in the admission agreement to the other party (and the guarantor to the admission agreement where relevant).

#### 4.2.2 Other Employers

An employer that is not an admission body may also become an exiting employer, for example as a result of the employer's last active member ceasing active membership in GMPF. However, the Administering Authority has the discretion to suspend the requirement for an exit payment (see 4.2.3. below) in specific circumstances where the relevant employer is likely to subsequently employ an active member within a period of no more than 3 years.

### 4.2.3 Exit payments

If an employer becomes an exiting employer under Regulation 64 of the 2013 LGPS Regulations, the Administering Authority may instruct the Actuary to carry out a special valuation to determine whether an exit payment is required from the employer.

The Administering Authority must look to protect the interests of other ongoing employers and will adopt valuation assumptions which, to the extent reasonably practicable, protect the other employers from the likelihood of any material loss emerging in future.

The assumptions adopted to value the exiting employer's liabilities for this valuation will therefore depend upon the circumstances. For example:

- (a) Where there is no guarantor to the exiting employer's admission agreement (or no admission agreement exists), 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" with no allowance for potential future investment outperformance and with an allowance for further future improvements in life expectancy. This approach results in a higher value being placed on the liabilities than would be the case under a valuation on the ongoing funding basis and could give rise to significant payments being required.
- (b) Where there is a guarantor to the exiting employer's admission agreement, it is possible that any deficit could be transferred to the guarantor. In some cases, particularly for Transferee Admission Bodies, the admission agreement may specify that all of the assets and liabilities in the admission body's sub-fund within GMPF will return to the sub-fund of the guarantor without needing to crystallise any deficit.

In other cases, the admission agreement may require the Administering Authority to seek repayment of the termination deficit from the exiting employer with any unpaid amounts then falling due on the guarantor. In such cases, a discussion may be held with the guarantor to determine the most appropriate basis for calculation and the timing of any deficit payments.

In all cases, GMPF's default position is that any termination deficit would be levied on the exiting employer as a capital payment.

In the event that GMPF is not able to recover the required payment in full directly from the exiting employer or from any bond, indemnity or guarantor, then:

- (a) In the case of Transferee Admission Bodies the awarding authority will be liable. At its absolute discretion, the Administering Authority may agree to recover any outstanding amounts via an increase in the awarding authority's contribution rate over an agreed period;
- (b) In the case of employers that are not Transferee Admission Bodies and have no guarantor, the unpaid amounts fall to be shared amongst all of the employers in the Fund. This will normally be reflected in contribution rates set at the formal valuation following the cessation date.

As an alternative to (b) above, where the exiting employer is continuing in business, GMPF, at its absolute discretion, reserves the right to enter into an agreement with the exiting employer to accept appropriate alternative security to be held against any deficit and to carry out the exit valuation on a less prudent valuation basis or recover the deficit over an agreed period.

This approach would be monitored as part of each triennial valuation and GMPF reserves the right to revert to a *gilts cessation basis* and seek immediate payment of any funding shortfall identified.

## 4.3 Employers with no remaining active members

In general an employer exiting GMPF due to the departure of the last active member, will pay an exit debt on an appropriate basis and consequently have no further obligation to GMPF. Thereafter it is expected that one of two situations will eventually arise:

- The employer's asset share runs out before all its ex-employees' benefits have been paid. In this situation the other employers in GMPF will be required to contribute to pay all remaining benefits: this will be done by the

Actuary apportioning the remaining liabilities on a pro-rata basis at successive formal valuations;

- 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 Actuary to the other GMPF employers.

#### 4.4 Early Retirement Costs

In the valuation process, it is assumed that active and deferred members' benefits on retirement will be payable from the earliest age that the member could retire without incurring a reduction to their benefit and without requiring their employer's consent to retire. Members receiving their pension unreduced before this age (or enhanced on ill health grounds) are deemed to have retired "early" and the expected cost of providing that member's benefits will increase.

Any additional lump sum contributions which are required to be made by the employer under Section 3.8 arising from early retirements become due immediately upon the award of an early retirement. The Administering Authority may in exceptional circumstances agree that an employer be permitted to spread the payment of ill health early retirement costs over a period of time.

GMPF monitors each employer's, or pool of employers', early retirement experience compared to the allowances described in section 3.8 on an ongoing basis. This information is used to determine any necessary lump sum employer contributions.

#### 4.5 Policies on bulk transfers

From time to time GMPF makes or receives a bulk transfer of members' accrued benefits from other LGPS funds or other occupational pension schemes ("external" transfer). GMPF also undertakes 'internal' bulk transfers, where the liabilities in respect of a group of members transfer from one employer to another. In the case of external transfers, the amount of assets transferred is determined in accordance with the LGPS Regulations. For internal transfers, the amount of assets is determined by the Actuary and Administering Authority in consultation with the ceding and receiving employer. Each case will be treated on its own merits, but in general:

- GMPF will seek the most cost effective method of transfer to keep professional and administration costs as low as possible;
- The maximum amount GMPF will pay on a bulk transfer is an amount equal to the asset share held by the transferring employee's employer and is capped at the value of the transferring employee's liabilities, measured on an appropriate actuarial basis;
- When a transfer takes place such that the transferring employer will no longer have any active membership then the transfer amount may be limited by the need for GMPF to meet the liabilities of any ex-employees of the employer;
- GMPF will not grant added benefits to members bringing in entitlements from another fund unless the asset transfer is sufficient to meet the added liabilities;
- GMPF may permit shortfalls to arise on bulk transfers if the employer has suitable strength of covenant and commits to meeting that shortfall in an appropriate period. This may require the employer's contributions to increase between valuations.

#### 4.6 Pay awards in excess of assumptions made by the Actuary

Some admission agreements state that GMPF reserves the right to seek additional contributions from admission bodies if pay awards have been in excess of the rate assumed by the Actuary at previous actuarial valuations. Prior to seeking any such payment GMPF will consult the relevant guarantor to the admission agreement.

#### 4.5 Policies on bulk transfers

From time to time GMPF makes or receives a bulk transfer of members' accrued benefits from other LGPS funds or other occupational pension schemes ("external" transfer). GMPF also undertakes 'internal' bulk transfers, where the liabilities in respect of a group of members transfer from one employer to another. In the case of external transfers, the amount of assets transferred is determined in accordance with the LGPS Regulations.

For internal transfers, the amount of assets is determined by the Actuary and Administering Authority in consultation with

the ceding and receiving employer. Each case will be treated on its own merits, but in general:

- GMPF will seek the most cost effective method of transfer to keep professional and administration costs as low as possible;
- The maximum amount GMPF will pay on a bulk transfer is an amount equal to the asset share held by the transferring employee's employer and is capped at the value of the transferring employee's liabilities, measured on an appropriate actuarial basis;
- When a transfer takes place such that the transferring employer will no longer have any active membership then the transfer amount may be limited by the need for GMPF to meet the liabilities of any ex-employees of the employer;
- GMPF will not grant added benefits to members bringing in entitlements from another fund unless the asset transfer is sufficient to meet the added liabilities;
- GMPF may permit shortfalls to arise on bulk transfers if the employer has suitable strength of covenant and commits to meeting that shortfall in an appropriate period. This may require the employer's contributions to increase between valuations.

#### 4.6. Pay awards in excess of assumptions made by the Actuary

Some admission agreements state that GMPF reserves the right to seek additional contributions from admission bodies if pay awards have been in excess of the rate assumed by the Actuary at previous actuarial valuations. Prior to seeking any such payment GMPF will consult the relevant guarantor to the admission agreement.

### 5. Links to investment strategy

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Funding and investment strategy are inextricably linked. Investment strategy is set by the Administering Authority, after consultation with the employers and after taking investment advice.

#### 5.1 Investment strategy

The investment strategies currently being pursued are described in GMPF's Investment Strategy Statement (formerly Statement of Investment Principles).

The investment strategies are set for the long-term, but the principal strategy (for the "Main Fund") is reviewed annually, to ensure that it remains appropriate to the relevant liability profile and takes account of major movements in market valuations. The Administering Authority has adopted a Main Fund benchmark, which sets the proportion of assets to be invested in key asset classes such as equities, bonds and property. As at 31 March 2016, the proportion to be held in equities and property was broadly 75% of the total Main Fund assets.

The investment strategy of lowest risk would be that which provides cashflows which replicate the expected benefit cashflows (i.e. the liabilities). Equity investment would not be consistent with this. This strategy informs policy for part of GMPF where liabilities are mature and employers have agreed such an approach.

The Main Fund's benchmark includes a significant holding in growth-seeking assets such as equities in the pursuit of long term higher returns than from a liability matching strategy. The Administering Authority's strategy recognises the relatively immature liabilities relevant to the Main Fund and the secure nature of most employers' covenants.

The same investment strategy is currently followed for all employers covered by the Main Fund. The Administering Authority can discuss with employers the feasibility of pursuing a more cautious investment strategy than the Main Fund norm.



## 5.2 Consistency with Funding Basis

For employers covered by the Main Fund, the funding basis adopts an asset outperformance assumption of 2.0% pa over and above the redemption yield on long term UK Government bonds. The Main Fund's current bespoke investment strategy is broadly 75% held in real assets and 25% in monetary assets. For employers pursuing a more cautious investment strategy than the Main Fund norm, a lower asset outperformance assumption may be adopted as appropriate. Both the Actuary and the investment adviser to GMPF consider that the funding basis fulfils the requirement to take a *prudent longer-term approach* to funding.

The Administering Authority is aware that in the short term – such as the three yearly assessments at formal valuations – the proportion of the assets invested in growth-seeking assets brings the possibility of considerable volatility and there is a material chance that in the short term, and even the medium term, asset returns will fall short of the outperformance target. The stability measures described in Section 3 will damp down, but not remove, the effect on employers' contributions.

GMPF does not hold a contingency reserve to protect it against the volatility of investments.

## 5.3 Balance between risk and reward

Prior to implementing its current investment strategies, the Administering Authority considered the balance between risk and reward by altering the level of investment in potentially higher returning, but more volatile asset classes, like equities. This process was informed by the use of asset-liability techniques to model the range of potential future solvency levels and contribution rates.

Being mindful of the sensitivity of individual employers' contributions to changes in investment returns, the Administering Authority continues to review the feasibility of implementing more bespoke investment strategies for individual employers or groups of employers. Enabling other investment strategies will require an increase in the number of investment mandates and potentially higher ongoing costs which would have to be borne by the employers. The potential benefits of multiple investment strategies need to be assessed against the costs.

## 5.4 Inter-valuation Monitoring of Funding Position

The Administering Authority monitors investment performance on a quarterly and annual basis. There is also detailed monitoring of additional liabilities arising from early and ill health retirements, the costs of which are met by employers. In addition, the Actuary routinely assesses the funding position, taking account of elements of actual experience compared to the financial assumptions underlying the valuation. Formally, the Administering Authority reports back to employers at the GMPF Annual General Meeting.

# 6. Key risks & controls

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## 6.1 Types of Risk

The Administering Authority has an active risk management programme in place. The measures that the Administering Authority has in place to control key risks are summarised below under the following headings:

- financial;
- demographic;
- regulatory; and
- governance

## 6.2 Financial risks

Risk	Summary of control mechanisms
Fund assets fail to deliver returns in line with the anticipated returns underpinning valuation of liabilities over the long term.	<p><i>Only anticipate long-term return on a relatively prudent basis to reduce risk of under-performing.</i></p> <p><i>Analyse progress at three yearly valuations for all employers.</i></p> <p><i>Use of interim valuations to monitor funding levels.</i></p>
Inappropriate long term investment strategy.	<p><i>Set GMPF-specific benchmark, informed by asset-liability modelling of liabilities.</i></p> <p><i>Examine scope for extending employer-specific investment strategies.</i></p> <p><i>Annual review of investment strategy incorporates consideration of alternative approaches.</i></p>
Fall in risk-free returns on Government bonds, leading to rise in value placed on liabilities.	<p><i>Some investment in bonds helps to mitigate this risk and there is scope for employers to increase bond exposure.</i></p>
Active investment manager under-performance relative to benchmark.	<p><i>Short term (quarterly) investment monitoring analyses market performance and active managers relative to their index benchmark.</i></p> <p><i>GMPF has implemented a manager monitoring framework.</i></p> <p><i>Regular reporting to employers describes Main Fund performance. If appropriate, the Actuary will be asked to evaluate the implications.</i></p>
Pay and price inflation significantly more than anticipated.	<p><i>The focus of the actuarial valuation process is on real returns on assets, net of price and pay increases.</i></p> <p><i>Inter-valuation monitoring, as above, gives early warning.</i></p> <p><i>Some investment in bonds, particularly index-linked bonds, also helps to mitigate this risk.</i></p> <p><i>Employers pay for the impact of their own salary awards and are reminded of the geared effect on pension liabilities of any bias in pensionable pay rises towards longer-serving employees.</i></p>

Risk	Summary of control mechanisms
Effect of possible increase in employer's contribution rate on service delivery and admission/ scheduled bodies.	<p><i>Seek feedback from employers on scope to absorb short-term contribution rises.</i></p> <p><i>Mitigate impact through deficit spreading and phasing in of contribution rises.</i></p> <p><i>Consult employers on possibility of paying more (extra administration and higher regular contributions) to enable employer-specific investment strategies to give greater certainty of cost.</i></p>
Orphaned employers give rise to added costs for GMPF.	<p><i>GMPF seeks a cessation debt (or security/guarantor) to minimise the risk of this happening in the future.</i></p> <p><i>If it occurs, the Actuary calculates the added cost spread pro-rata among all employers.</i></p>

### 6.3 Demographic risks

Risk	Summary of control mechanisms
Pensioners living longer.	<p><i>Set mortality assumptions with some allowance for future increases in life expectancy.</i></p> <p><i>Actuary monitors experience of a large sample of pension funds when setting assumptions and makes allowance for the location and lifestyle of GMPF's membership.</i></p>
Deteriorating patterns of ill health and other early retirements.	<p><i>Employer contribution rates include an allowance to help meet the strains that arise from ill health early retirement costs.</i></p> <p><i>Early retirement experience and its financial impact are measured on an ongoing basis.</i></p>

### 6.4 Regulatory risks

Risk	Summary of control mechanisms
Changes to regulations, e.g. more favourable benefits package.	<p><i>The Administering Authority is alert to the potential creation of additional liabilities and administrative difficulties for employers and itself.</i></p>
Changes to national pension requirements and/or HM Revenue and Customs rules e.g. changes arising from Public Sector Reform.	<p><i>The Administering Authority considers all consultation papers issued by MHCLG/HM Treasury and comments where appropriate.</i></p> <p><i>It will consult employers where it considers that it is appropriate.</i></p> <p><i>Any changes to member contribution rates or benefit levels will be carefully communicated with members to minimise possible opt-outs or adverse actions.</i></p> <p><i>Copies of all submissions are available for employers to see at <a href="http://www.gmpf.org.uk">www.gmpf.org.uk</a></i></p>

## 6.5 Governance risk

Risk	Summary of control mechanisms
Administering Authority unaware of structural changes in an employer's membership (e.g. large fall in employee members, large number of retirements).	<p><i>The Administering Authority monitors membership movements on an annual basis, via a report from the administrator to the Pension Fund Management Panel.</i></p> <p><i>The Administering Authority and Actuary will be involved in actioning any bulk transfer of members from an employer's sub-fund and will consider any subsequent risks.</i></p>
Administering Authority not advised of an employer closing to new entrants.	<p><i>The Actuary may be instructed to consider revising the rates and Adjustments certificate to increase an employer's contributions (under Regulation 64) between triennial valuations.</i></p> <p><i>Deficit contributions may be expressed as monetary amounts (see Actuarial Valuation report).</i></p>
Administering Authority failing to commission the Actuary to carry out a termination valuation for a departing Admission Body and losing the opportunity to call in a debt.	<p><i>In addition to the Administering Authority monitoring membership movements on an annual basis, it requires employers with Admission Agreements to inform it of forthcoming changes.</i></p> <p><i>It also operates a diary system to alert it to the forthcoming termination of Transferee Admission Agreements.</i></p>
An employer ceasing to exist with insufficient funding or adequacy of a bond.	<p><i>The Administering Authority believes that it would normally be too late to address the position if it was left to the time of departure.</i></p> <p><i>The risk is mitigated by:</i></p> <ul style="list-style-type: none"> <li>● <i>Seeking a funding guarantee from another scheme employer, or external body, wherever possible.</i></li> <li>● <i>Alerting the prospective employer to its obligations and encouraging it to take independent actuarial advice.</i></li> <li>● <i>Vetting prospective employers before admission.</i></li> <li>● <i>Offering lower risk investment strategies – with higher employer contributions - to reduce the risk of investment under performance and a significant debt crystallising on termination.</i></li> </ul>

## 7. Definitions

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### Solvency

The notes to the Public Service Pensions Act 2013 state that solvency means that the rate of employer contributions should be set at “such level as to ensure that the scheme’s liabilities can be met as they arise”. It is not regarded that this means that the pension fund should be 100% funded at all times. Rather, and for purposes of Section 13 of the Public Service Pensions Act 2013, the rate of employer contributions shall be deemed to have been set at an appropriate level to ensure solvency 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 either
- 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
- there is an appropriate plan in place should there be, or if there is expected in future to be, a limited number of fund employers, or a material reduction in the capacity of fund employers to increase contributions as might be needed.

If the conditions above are met, then it is expected that the fund will be able to pay scheme benefits as they fall due.

### Long term cost efficiency

The notes to the Public Service Pensions Act 2013 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.”

The rate of employer contributions shall be deemed to have 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.

In assessing whether the above condition is met, GAD may have regard to the following considerations:

- The implied average deficit recovery period.
- The investment return required to achieve full funding over different periods e.g. the recovery period.
- If there is no deficit, the extent to which the amount of contributions payable is likely to lead to a deficit arising in the future.
- The extent to which the required investment return is less than the administering authority’s view of the expected future return being targeted by a fund’s investment strategy taking into account changes in maturity/strategy as appropriate.

*End of main body of FSS*

*Adopted by the Pension Fund Management Panel: 10 March 2017*



## ANNEX - Responsibilities of key parties

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### The Administering Authority should:

- operate GMPF as per the LGPS Regulations;
- effectively manage any potential conflicts of interest arising from its dual role as Administering Authority and a GMPF employer;
- collect employer and employee contributions, and investment income and other amounts due;
- ensure that cash is available to meet benefit payments as and when they fall due;
- pay from GMPF the relevant benefits and entitlements that are due;
- invest surplus monies (i.e. contributions and other income which are not immediately needed to pay benefits) in accordance with GMPF's Investment Strategy Statement (formerly Statement of Investment Principles and LGPS Regulations);
- communicate appropriately with employers so that they fully understand their obligations to GMPF;
- take appropriate measures to safeguard GMPF against the consequences of employer default;
- manage the valuation process in consultation with GMPF's actuary;
- prepare and maintain a FSS and a ISS/SIP, after consultation;
- notify the Actuary of material changes which could affect funding; and
- monitor all aspects of GMPF's performance and funding and amend the FSS and ISS/SIP as necessary and appropriate.

### The Individual Employer should:

- deduct contributions from employees' pay correctly;
- pay all contributions, including their own as determined by the Actuary, promptly by the due date;
- exercise discretions within the regulatory framework;
- make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of scheme benefits, early retirement strain; and
- notify the Administering Authority promptly of all proposed material changes to membership or legal status which affect future funding.

### The Actuary should:

- 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;
- provide advice relating to new employers in GMPF, including the level and type of bonds or other forms of security (and the monitoring of these);
- prepare advice and calculations in connection with bulk transfers and individual benefit related matters;
- assist the Administering Authority in considering possible changes to employer contributions between formal valuations, where circumstances suggest this may be necessary;
- advise on the termination of Admission Bodies' participation in GMPF; and
- fully reflect actuarial professional guidance and requirements in the advice given to the Administering Authority.

## Other parties:

- investment advisers (either internal or external) may be asked to assist in ensuring that GMPF's ISS/SIP remains appropriate, and consistent with this FSS;
- investment managers, custodians and bankers will typically all play their part in the effective investment (and dis-investment) of GMPF assets, in line with the ISS/SIP;
- auditors will comply with their auditing standards and sign off annual reports and financial statements as appropriate;
- the Local Pensions Board will review the valuation process and funding strategy and ensure they comply with the regulations and relevant guidance.
- The LGPS Scheme Advisory Board and the Government Actuary will also review GMPF's funding strategy as part of their monitoring of the LGPS as a whole.