CHESHIRE PENSION FUND

Funding Strategy Statement

11 SEPTEMBER 2020

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CHESHIRE PENSION FUND

1. Introduction

1.1 What is this document?

This is the Funding Strategy Statement (FSS) of the Cheshire Pension Fund ("the Fund"), which is administered by Cheshire West and Chester Council, ("the Administering Authority").

It has been prepared by the Administering Authority in collaboration with the Fund's actuary, Hymans Robertson LLP, and after consultation with the Fund's employers and investment adviser. It is effective from 13 March 2020.

1.2 What is the Cheshire Pension Fund?

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

Cheshire West & Chester Council as the Administering Authority runs the Cheshire Pension Fund to make sure the Fund:

- receives the proper amount of contributions from employees and employers, and any transfer payments;
- invests the contributions appropriately, with the aim that the Fund's assets grow over time with investment income and capital growth; and
- uses the assets to pay pensions and benefits due to the members and to their dependants as defined in the LGPS Regulations. Assets are also used to pay transfer values and administration costs.

The roles and responsibilities of the key parties involved in the management of the Fund are summarised in Appendix B.

1.3 Why does the Fund need a Funding Strategy Statement?

Employees' benefits are guaranteed by the LGPS Regulations, and do not change with market values or employer contributions. Employees' contributions are fixed in those Regulations also, at a level which covers only part of the cost of the benefits.

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

The FSS focuses on how employer pension liabilities are measured, the pace at which these liabilities are funded, and how employers or groups of employers (known as pools) pay for their own liabilities.

This statement sets out how the Administering Authority has balanced the conflicting aims of:

- affordability of employer contributions,
- transparency of processes,
- stability of employers' contributions over time, and
- prudence in the funding basis

There are also regulatory requirements for an FSS, as given in Appendix A.

The FSS forms part of a governance framework which includes:

- the LGPS Regulations;
- the Rates and Adjustments Certificate issued by the Fund's appointed actuary Hymans Robertson (confirming employer contribution rates from 1 April 2020) which can be found in an appendix to the formal valuation report;
- the Fund's policy on admission or cessation of employers and bulk transfers;
- actuarial factors for valuing individual transfers, early retirement costs and the costs of buying added service; and
- the Fund's Investment Strategy Statement (see Section 4) Funding strategy and links to investment strategy

1.4 How does the Fund and this FSS affect me?

This depends who you are:

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

1.5 **What does the FSS do?**

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

- to ensure the long-term solvency of the Fund, using a prudent long term view. This will ensure that sufficient funds are available to meet all members' and dependants' benefits as they fall due for payment;
- to ensure that employer contribution rates are reasonably stable and affordable where appropriate;
- to minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return (**NB** this will also minimise the costs to be borne by Council Tax payers);
- to reflect the different characteristics of different employers in determining contribution rates.

This involves the Fund having a clear and transparent funding strategy to demonstrate how each employer can best meet its own liabilities over future years; and

- to use reasonable measures to reduce the risk to other employers and ultimately to the Council Tax payer from an employer defaulting on its pension obligations.

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

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

In Section 3 we outline how the Fund calculates the contributions payable by different employers in different situations.

In Section 4 we show how the funding strategy is linked with the Fund's investment strategy.

In the Appendices we cover various issues in more detail if you are interested:

A. the regulatory background, including how and when the FSS is reviewed,
B. who is responsible for what,
C. what issues the Fund needs to monitor, and how it manages its risks,
D. some more details about the actuarial calculations required,
E. the assumptions which the Fund actuary currently makes about the future,
F. the detailed explanatory notes to accompany Table 3.3
G. a glossary explaining the technical terms occasionally used in this FSS

If you have any other queries please email pensions@cheshirewestandhester.gov.uk

2. Basic funding issues

2.1 How does the actuary calculate the required contribution rate?

In essence this is a three-step process:

Step 1: Set the funding target for that employer, i.e. the estimated amount of assets it should hold in order to be able to pay all its members' benefits. See Appendix E for more details of what assumptions we make to determine that funding target;

Step 2: Determine the time horizon over which the employer should aim to achieve that funding target. See the table in 3.3 and Note (c) for more details;

Step 3: Calculate the employer contribution rate such that it has at least a given likelihood of achieving that funding target over that time horizon, allowing for various possible economic outcomes over that time horizon. See 2.3 below, and the table in 3.3 Note (e) for more details.

2.2 How is each employer's contribution rate presented?

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

a) The "Primary Rate": the estimated cost of benefits being built up each year, less members' own contributions and including an allowance for administration expenses. This is expressed as a percentage of members' pensionable pay; plus

b) The "Secondary Rate": an adjustment, if needed, to fund the cost of benefits already accrued before the valuation date. The Secondary Rate may be expressed as a percentage of pay and/or a monetary amount in each year.

The Primary and Secondary rates for all employers are shown in the Fund's Rates and Adjustments Certificate, which forms part of the formal Actuarial Valuation Report. Employers' contributions are expressed as the minimum payable, with employers able to pay contributions at a higher rate. Account of any higher rate will be will be reflected as a credit by the Actuary when next calculating the employer's contributions.

2.3 What different types of employers participate in the Fund?

Historically the LGPS was intended for local authority employees only. However over the years, with the diversification and changes to delivery of local services, many more types and numbers of employers now participate.

Whilst local authorities are still the largest participating employers, the LGPS also includes employers providing services in place of, or alongside, local authority services: academy schools, contractors, housing associations, charities, etc. There are currently more employers in the Fund than ever before, a significant part of this being due to the establishment of new academies.

In essence, participation in the LGPS is open to public sector employers providing some form of service to the local community.

The LGPS Regulations define various types of employer as follows:

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

- It is possible for Local Education Authority schools to convert to academy status, and for other forms of school (such as Free Schools) to be established. **Academies (or Multi Academy Trusts)**, become separate employers in the Fund. As academies are defined in the LGPS Regulations as “Scheduled Bodies”, the Administering Authority has no discretion over whether to admit them to the Fund, and the academy has no discretion whether to continue to allow its non-teaching staff to join the Fund..

- **Designating employers** - employers such as Town and Parish councils are able to participate in the LGPS by passing a resolution that they wish to join. The Administering Authority cannot refuse them entry where the resolution is passed. These employers “designate” which of their employees are eligible to join the scheme.

- **Admission Bodies:** Other employers who are able to participate in the Fund via what’s called an Admission Agreement in which the employer nominates the employees who it wants to have access to the LGPS. The Administering Authority sets out its criteria for participation by these employers in the Fund’s Admissions Policy and can refuse entry if these requirements are not met. There are two types of admission bodies
  - Employers who have a “community of interest” with another Scheduled Body in the Fund, often called – **community admission bodies** (“CAB”). CABs will include housing associations and charities
  - Employers providing a service under contract with a Scheduled Body, often called **transferee admission bodies** (“TAB)

2.4 How does the contribution rate vary for different employers?

All three steps in Section 2.2 are considered when setting contributions (more details are given in Section 3 and Appendix D).

The **funding target** is based on a set of assumptions about the future, (e.g. investment returns, inflation, pensioners' life expectancies). If an employer is approaching the end of its participation in the Fund then its funding target may be set on a more prudent basis, so that its liabilities are less likely to be spread among other employers after its cessation;

The **time horizon** is the period given to reach the funding target. Employers may be given a lower time horizon if they have a less permanent anticipated membership, or do not have tax-raising powers to increase contributions if investment returns under-perform; and

The **likelihood of success** of achieving the funding target over that time horizon will be dependent on the Fund's view of the strength of employer covenant and its funding profile. Where an employer is considered to be weaker then the required likelihood will be set higher, which in turn will increase the required contributions (and vice versa).

For some employers it may be agreed to pool contributions, see 3.5.

Any costs of non-ill-health early retirements must be paid by the employer, see 3.6.

Costs of ill-health early retirements are covered in 3.7 and 3.8.

2.5 How is an employer's funding level calculated?

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

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

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

It is important to note that the deficit/surplus and funding level are only measurements at a particular point in time, on a particular set of assumptions about the future. For most employers the key issue is how likely it is that their contributions will be sufficient to pay for their members' benefits.

2.6 **How does the Fund recognise that employer contribution rates can affect council and employer budgets , and council tax?**

The Administering Authority and the Fund actuary are acutely aware that, all other things being equal, higher contributions paid to the Fund may mean less cash available for the employer to spend on the provision of services.

It should also be borne in mind that:

- The Fund provides invaluable financial security to local families, whether to those who formerly worked in the service of the local community who have now retired, or to their families after their death;
- Lower contributions today will mean higher contributions tomorrow: deferring payments does not alter the employer's ultimate obligation to the Fund in respect of its current and former employees;
- Each employer will generally only pay for its own employees and ex-employees (and their dependants), not for those of other employers in the Fund;
- The Fund strives to maintain reasonably stable employer contribution rates where appropriate and possible. However, a recent shift in regulatory focus means that solvency within each generation is considered by the Government to be a higher priority than stability of contribution rates. For example, if stability of rates means that solvency isn't achieved within the current generation (which the Fund views as around 20 years), then it may not be possible to keep rates stable;
- The Fund wishes to avoid the situation where an employer's contributions fall so far behind that any deficit becomes unmanageable in practice: such a situation may lead to employer insolvency and the resulting deficit falling on the other Fund employers. In that situation, those other employers' services may in turn suffer as a result;

Overall, therefore, there is clearly a balance to be struck between the Fund's need for maintaining prudent funding levels, and the employers' need to allocate their resources appropriately. The Fund achieves this through various techniques which affect contribution rate changes to various degrees (see 3.1). In deciding which of these techniques to apply to any given employer, the Administering Authority takes a view on the financial standing of the employer.

The Administering Authority will make a risk assessment of that employer using a knowledge base which is regularly monitored and kept up-to-date. This assessment will include such information as the type of employer, its membership profile and funding position, financial standing, any guarantors or security provision, material changes anticipated, etc.

For instance, where the Administering Authority has confidence that an employer will be able to meet its funding commitments then the Fund will permit options such as stabilisation (see 3.3 Note (b)), a longer time horizon relative to other employers, and/or a lower likelihood of achieving their funding target. This is permitted in the expectation that the employer will still be able to meet its obligations for many years to come.

On the other hand, where there is doubt that the employer will be able to meet its funding commitments or withstand a significant change in its funding commitments then a higher funding target, and/or a shorter time horizon relative to other employers, and/or a higher likelihood of achieving the target may be required.

The Fund actively seeks employer input, including to its funding arrangements, through various means: see Appendix A.

2.7 What approach has the Fund taken to dealing with uncertainty arising from the McCloud court case and its potential impact on the LGPS benefit structure?

The courts have ruled that the 'transitional' protections' awarded to some members of public service pension schemes when the schemes were reformed (on 1 April 2014 in the case of the LGPS) were unlawful on the grounds of age discrimination.

At the time of writing the Ministry for Housing, Communities and Local Government (MHCLG) has not provided details of any changes to LGPS benefits as a result of the case. However, it is expected that benefit changes will be required and they will likely increase the value of liabilities. At present, the scale and nature of any increase in liabilities are unknown, which limits the ability of the Fund to make an accurate allowance.

The LGPS Scheme Advisory Board (SAB) issued advice to LGPS funds in May 2019 on the treatment of the McCloud case in valuations in the event there was no finalised outcome by 31 August 2019. The Fund Actuary has acted in line with SAB's advice and valued all member benefits in line with the current LGPS Regulations.

The Fund, in line with the advice in SAB's note, has considered how to allow for the "McCloud" risk in the setting of employer contribution rates and has taken the following approach:

- increase the prudence in the funding strategy via a higher likelihood of meeting funding target for the Councils who make up the majority of the Fund, and
- make no allowance for the smaller employers until the actual McCloud rectification is known except where there is a cessation valuation

As the majority of employers in the Fund are long term participants, the Fund will have time to make future adjustments as detail on the McCloud remedy emerges. The Fund should reserve the right to adjust employer contribution rates between formal valuations if deemed appropriate and necessary once the remedy to McCloud is known.

2.8 When will the next actuarial valuation be?

On 8 May 2019 MHCLG issued a consultation seeking views on (among other things) proposals to amend the LGPS valuation cycle in England and Wales from a three year (triennial) valuation cycle to a four year (quadrennial) valuation cycle.

At the time of writing, whilst the outcome of the consultation is unknown, MHCLG has confirmed that the next valuation will be carried out in three years in March 2022. The Fund has therefore instructed the Fund Actuary to certify contribution rates for employers for the period 1 April 2020 to 31 March 2023 as part of the 2019 valuation of the Fund.

3. Calculating contributions for individual employers

3.1 General comments

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

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

These and associated issues are covered in this Section.

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

3.2 The effect of paying lower contributions

In limited circumstances the Administering Authority may permit employers to pay contributions at a lower level than is assessed for the employer using the three step process above. At their absolute discretion the Administering Authority may:

- extend the time horizon for targeting full funding;
- adjust the required likelihood of success of meeting the funding target;
- permit an employer to participate in the Fund's stabilisation mechanisms;
- permit extended phasing in of contribution rises or reductions;
- pool contributions amongst employers with similar characteristics; and/or
- accept some form of security or guarantee in lieu of a higher contribution rate than would otherwise be the case.

Employers which are permitted to use one or more of the above methods will often be paying, for a time, contributions less than required to meet their funding target, over the appropriate time horizon with the required likelihood of success. Such employers should appreciate that:

- their true long term liability (i.e. the actual eventual cost of benefits payable to their employees and ex-employees) is not affected by the pace of paying contributions;
- lower contributions in the short term may lead to higher contributions in the long term; and
- it may take longer to reach their funding target, all other things being equal.

Overleaf (section 3.3) is a summary of how the main funding policies differ for different types of employer. More detailed notes where necessary are show in in Appendix F.

Section 3.4 onwards deals with various other funding issues which apply to all employers

3.3 **The different approaches used for different employers (See also Notes in Appendix F)**

Type of employer	**Scheduled Bodies**			**Community Admission Bodies and Designating Employers**		**Transferee Admission Bodies***
Sub-type	**Local Authorities, Police, Fire, Parish and Town Councils**	**Further Education Establishments**	**Academies**	**Open to new entrants**	**Closed to new entrants**	**(all)**
Funding Target Basis used	Ongoing participation basis, assumes long-term Fund participation (see Appendix E)			Ongoing, but may move to "gilts basis" - see Note (a)		Contractor exit basis, assumes fixed contract term
Primary rate approach	(see Appendix D – D.2)					
Stabilised contribution rate?	Yes - see Note (b)	No	No	No	No	No
Maximum time horizon – Note (c)	20 years	15 years	20 years	15 years	15 years	Outstanding contract term
Secondary rate – Note (d)	Monetary amount for 4 main Councils ,% of payroll for	Monetary amount	% of payroll	Monetary amount	Monetary amount	Monetary amount

Type of employer	Scheduled Bodies			Community Admission Bodies and Designating Employers		Transferee Admission Bodies*
Treatment of surplus	Covered by stabilisation arrangement	Preferred approach: contributions kept at primary rate. However reductions may be permitted by the Administering Authority on a case by case basis	Preferred approach: contributions kept at primary rate. However reductions may be permitted by the Administering Authority on a case by case	Preferred approach: contributions kept at primary rate. However, reductions may be permitted by the Admin. Authority on a case-by-case basis		Reduce contributions by spreading the surplus over the remaining contract term
Likelihood of Success of achieving target – Note (e)	66%	75% but may reduce in return for added security see note 3.6	66%	75% but may reduce in return for added security see note 3.6	75% but may reduce in return for added security see note 3.6	66%
Phasing of contribution changes	Covered by stabilisation arrangement	may be permitted by the Administering Authority on a case by case basis	may be permitted by the Administering Authority on a case by case basis	may be permitted by the Administering Authority on a case by case basis	None	None
Review of rates – Note (f)	Administering Authority reserves the right to review contribution rates and amounts, and the level of security provided, at regular intervals between valuations					Particularly reviewed in last 3 years of contract

New employer	n/a	n/a	Note (g)	Note (h)	Notes (h) & (i)

Cessation of participation: cessation debt/surplus payable	Cessation is assumed not to be generally possible, as Scheduled Bodies are legally obliged to participate in the LGPS. In the rare event of cessation occurring (machinery of Government changes for example), the cessation debt principles applied would be as per Note (j).	Can be ceased subject to terms of admission agreement. Exit debt/credit will be calculated on a basis appropriate to the circumstances of cessation – see Note (j).	Participation is assumed to expire at the end of the contract. Exit debt/credit will be calculated on a basis appropriate with the circumstances of cessation - see Note (j). Letting employer will be liable for future deficits and contributions arising. See Note (j) for further details.

*Where the Administering Authority recognises a fixed contribution rate agreement between a letting authority and a contractor, the certified employer contribution rate will be derived in line with the methodology specified in the risk sharing agreement. Additionally, in these cases, upon cessation the contractor's assets and liabilities will transfer back to the awarding authority with no crystallisation of any deficit or surplus. Further detail on fixed contribution rate agreements is set out in note (i).

3.4 **Draft overview of employer framework for 2019 valuation**

3.5 **Pooled contributions**

Each employer will generally only pay for its own employees and ex-employees (and their dependants) not for those of other employers in the Fund. However, from time to time the Administering Authority may set up pools for employers with similar characteristics. This will always be in line with its broader funding strategy.

The intention of such employer pools is to minimise contribution rate volatility which would otherwise occur when members join, leave, take early retirement, receive pay rises markedly different from expectations, etc. Such events can cause large changes in contribution rates for very small employers in particular, unless these are smoothed out for instance by pooling across a number of employers.

The employers in the pool will still have their own individual funding positions tracked by the Actuary, so that some employers will be much better funded, and others much more poorly funded, than the pool average.

The main purpose of pooling is to produce more stable employer contribution levels in the longer term whilst, recognising that ultimately there will be some level of cross-subsidy of pension cost amongst pooled employers

Community Admission Bodies and Transferee Admission Bodies are not permitted to participate in a pool.

With the advice of the Actuary the Administering Authority has allowed Parish and Town Councils to pool for the purposes of setting contributions. The underlying funding position of each Parish and Town Council continues to be tracked.

Employers who are permitted to enter (or remain in) a pool at the 2019 valuation will not normally be advised of their individual contribution rate unless agreed by the Administering Authority.

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

3.6 **Additional flexibility in return for added security**

The Administering Authority may permit greater flexibility to the employer's contributions if the employer provides added security to the satisfaction of the Administering Authority.

Such flexibility may include setting a lower likelihood of success of achieving the funding target, a reduced rate of contributions or an extended time horizon.

Such security may include, but is not limited to, a suitable bond, a legally-binding guarantee from an appropriate third party, or security over an employer asset of sufficient value. The degree of flexibility given may take into account factors such as:

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

3.7 **Non ill health early retirement costs**

Employers are required to pay additional contributions ('pension strain') wherever an employee retires before attaining the age at which they can take their benefits without incurring a reduction. The actuary's funding basis makes no allowance for early retirement except on grounds of ill-health.

Strain costs must be paid in full in the year in which the strain is incurred.

The Administering Authority at its sole discretion may allow the strain payment to be spread over a period not to exceed 3 years.

3.8 **Ill health early retirement costs**

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

The Actuary makes provision, known as an 'ill health allowance' into the employer's contribution rate set at each actuarial valuation.

The Administering Authority is notified of the cash value of this "ill-health allowance" from the actuary for the period covered by the actuarial valuation. Where an employer does not take out ill- health insurance, they may be invoiced for any cumulative ill-health retirement costs over their allowance.

3.9 **External Ill health insurance**

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

- the employer's contribution to the Fund each year is reduced by the amount of that year's insurance premium, so that the total cost of is unchanged, and
- there is no need for monitoring of allowances.

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

3.10 Employers with no remaining active (employee) members

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

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

a) The employer's asset share runs out before all its ex-employees' benefits have been paid. In this situation the other Fund employers will indirectly contribute to pay all remaining benefits. This will be done by the Fund actuary apportioning the remaining liabilities on a pro-rata basis at successive formal valuations;

b) The last ex-employee or dependant dies before the employer's asset share has been fully utilised. In this situation the remaining assets would be apportioned pro-rata by the Fund's actuary to the benefit of other Fund employers.

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

3.11 Policies on bulk transfers

This section covers bulk transfer payments into, out of and within the Fund.

A bulk transfer is a special arrangement whereby transfer terms apply to members transferring their pension benefits in bulk to a new employer's scheme and receive benefits of equivalent value.

Each case will be treated on its own merits, but in general:

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

4. Funding strategy and links to investment strategy

4.1 What is the Fund's investment strategy?

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

Investment strategy is set by the Administering Authority, after consultation with the employers and after taking investment advice. The precise mix, manager make up and target returns are set out in the Investment Strategy Statement, which is available to members and employers.

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

Currently there are four investment strategies in the Fund, with a range of allocation to growth assets. More detail of these strategies are set out in the Investment Strategy Statement.

Employers are allocated by the Administering Authority and the Fund's Strategic Investment Advisor to the investment strategy which is most appropriate given the employer's funding objective and current funding position.

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

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

Therefore, the funding and investment strategies are inextricably linked.

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

In the opinion of the Fund actuary, the current funding strategy is consistent with the current investment strategy of the Fund. The actuary's assumption for future investment returns (described further in Appendix E) are based on the current benchmark investment strategies of the Fund. The future investment return assumptions underlying each of the Fund's three funding bases included a margin for prudence, and are there considered to be consistent with the requirement to take a "prudent longer-term view" of the funding of liabilities as required by the UK Government (see Appendix A1).

In the short term – such as the period between formal valuations – there is the scope for considerable volatility in asset values. However, the actuary takes a long term view when assessing employer contribution rates (where appropriate) and the contribution rate setting methodology takes into account this potential variability.

The Fund does not hold a contingency reserve to protect it against the volatility of equity investments.

4.4 Does the Fund monitor its overall funding position?

The Administering Authority monitors the relative funding position, i.e. changes in the relationship between asset values and the liabilities value, monthly. It reports this to the regular Pensions Committee meetings, and also to employers from time to time.

The estimated funding level of any employer in the Fund can be provided by the Administering Authority within 5 business days of request.

5. Statutory reporting and comparison to other LGPS Funds

5.1 Purpose

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

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

5.2 Solvency

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

(a) the rate of employer contributions is set to target a funding level for the Fund of 100%, over an appropriate time period and using appropriate actuarial assumptions (where appropriateness is considered in both absolute and relative terms in comparison with other funds); and either

(b) employers collectively have the financial capacity to increase employer contributions, and/or the Fund is able to realise contingent assets should future circumstances require, in order to continue to target a funding level of 100%; or

(c) there is an appropriate plan in place should there be, or if there is expected in future to be, a material reduction in the capacity of fund employers to increase contributions as might be needed.

5.3 Long Term Cost Efficiency

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

i. the rate of employer contributions is sufficient to make provision for the cost of current benefit accrual,

ii. with an appropriate adjustment to that rate for any surplus or deficit in the Fund.

In assessing whether the above condition is met, MHCLG may have regard to various absolute and relative considerations. A relative consideration is primarily concerned with comparing LGPS pension funds with other LGPS pension funds. An absolute consideration is primarily concerned with comparing Funds with a given objective benchmark.

Relative considerations include:

1. the implied deficit recovery period; and
2. the investment return required to achieve full funding after 20 years.

Absolute considerations include:

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

MHCLG may assess and compare these metrics on a suitable standardised market-related basis, for example where the local funds’ actuarial bases do not make comparisons straightforward.

Appendix A – Regulatory framework

A1. Why does the Fund need an FSS?

The Ministry of Housing, Communities and Local Government (MHCLG) has stated that the purpose of the FSS is:

- *"to establish a **clear and transparent fund-specific strategy** which will identify how employers' pension liabilities are best met going forward;*
- *to support the regulatory framework to maintain **as nearly constant employer contribution rates as possible**; and*
- *to take a **prudent longer-term view** of funding those liabilities."*

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

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

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

A2. Does the Administering Authority consult anyone on the FSS?

Yes. This is required by LGPS Regulations. It is also covered in more detail by the most recent CIPFA (Chartered Institute of Public Finance & Accountancy) guidance, which states that the FSS must first be subject to "consultation with such persons as the authority considers appropriate", and should include "a meaningful dialogue at officer and elected member level with council tax raising authorities and with corresponding representatives of other participating employers".

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

a) A draft version of the FSS was issued to all participating employers on 20 December 2019 for comment;

b) Comments were requested by 24 January 2020

c) Following the end of the consultation period the FSS was updated where required, approved by the Pension Fund Committee and then published, on 13 March 2020

A3. How is the FSS published?

The FSS is made available through the following routes:

- Published on the website, at www.cheshirepensionfund.org;
- A copy sent by e-mail to each participating employer in the Fund;
- A copy sent to the Pension Fund Committee and Local Pension Board;
- A full copy included in the annual report and accounts of the Fund;
- Copies sent to investment managers and independent advisers;
- Copies made available on request.

A4. How often is the FSS reviewed?

The FSS is reviewed in detail at least at every formal valuation (if not more frequently). This version is expected to remain unaltered until it is consulted upon as part of the formal process for the next valuation.

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

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

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

A5. How does the FSS fit into other Fund documents?

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

These documents can be found on the web at www.cheshirepensionfund.org

Appendix B – Responsibilities of key parties

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

B1. The Administering Authority should:-

- operate the Fund as per the LGPS Regulations;
- effectively manage any potential conflicts of interest arising from its dual role as Administering Authority and a Fund employer;
- collect employer and employee contributions, and investment income and other amounts due to the Fund;
- ensure that cash is available to meet benefit payments as and when they fall due;
- pay from the Fund 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 the Fund's Investment Strategy Statement (ISS) and LGPS Regulations;
- communicate appropriately with employers so that they fully understand their obligations to the Fund;
- take appropriate measures to safeguard the Fund against the consequences of employer default;
- manage the valuation process in consultation with the Fund's actuary;
- provide data and information as required by the Government Actuary's Department to carry out their statutory obligations (see Section 5);
- prepare and maintain a FSS and a ISS, after consultation;
- notify the Fund's actuary of material changes which could affect funding (this is covered in a separate agreement with the actuary); and
- monitor all aspects of the fund's performance and funding and amend the FSS and ISS as necessary and appropriate.

B2. 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;
- have a policy and 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 changes to its circumstances, prospects or membership, which could affect future funding.

B3. The Fund 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 data and information as required by the Government Actuary's Department to carry out their statutory obligations (see Section 5);
- provide advice relating to new employers in the Fund, including the level and type of bonds or other forms of security (and the monitoring of these);
- 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 employers' participation in the Fund; and
- fully reflect actuarial professional guidance and requirements in the advice given to the Administering Authority.

B4. Other parties:-
- investment advisers (either internal or external) should ensure the Fund's ISS remains appropriate, and consistent with this FSS;
- investment managers, custodians and bankers should all play their part in the effective investment (and dis-investment) of Fund assets, in line with the ISS;
- auditors should comply with their auditing standards, ensure Fund compliance with all requirements, monitor and advise on fraud detection, and sign off annual reports and financial statements as required;
- governance advisers may be appointed to advise the Administering Authority on efficient processes and working methods in managing the Fund;
- legal advisers (either internal or external) should ensure the Fund's operation and management remains fully compliant with all regulations and broader local government requirements, including the Administering Authority's own procedures;
- MHCLG (assisted by the Government Actuary's Department) and the Scheme Advisory Board, should work with LGPS Funds to meet Section 13 requirements.

Appendix C – Key risks and controls

C1. Types of risk

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

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

C2. Financial risks

Financial Risk	Summary of Control Mechanisms
Fund assets fail to deliver returns in line with the anticipated returns underpinning contribution rates and the valuation of liabilities over the long- term.	Only anticipate long-term returns on a relatively prudent basis to reduce risk of under-performing. Assets invested on the basis of specialist advice, in a suitably diversified manner across asset classes, geographies, managers, etc. Analyse progress at formal valuations for all employers. Inter-valuation roll-forward of liabilities between valuations at whole Fund level.
Inappropriate long-term investment strategy.	Overall investment strategy options considered as an integral part of the funding strategy. Used asset liability modelling to measure 4 key outcomes. Chosen option considered to provide the best balance. Operation of multiple investment strategies to meet needs of a diverse employer group.
Fall in risk-free returns on Government bonds, leading to rise in value placed on liabilities.	Stabilisation modelling at whole Fund level allows for the probability of this within a longer term context. Inter-valuation monitoring, as above. Some investment in bonds helps to mitigate this risk.
Active investment manager under-performance relative to benchmark.	Quarterly investment monitoring analyses market performance and active managers relative to their index benchmark.

Financial Risk	Summary of Control Mechanisms
Pay and price inflation significantly more than anticipated.	The focus of the actuarial valuation process is on real returns on assets, net of price and pay increases. Inter-valuation monitoring, as above, gives early warning. Some investment in bonds also helps to mitigate this risk. Employers pay for their own salary awards and should be mindful of the geared effect on pension liabilities of any bias in pensionable pay rises towards longer-serving employees.
Effect of possible increase in employer's contribution rate on service delivery and admission/scheduled bodies	An explicit stabilisation mechanism has been agreed as part of the funding strategy. Other measures are also in place to limit sudden increases in contributions.
Orphaned employers give rise to added costs for the Fund	The Fund seeks a cessation payment (or security/guarantor) to minimise the risk of this happening in the future. If it occurs, the Actuary calculates the added cost spread pro-rata among all employers – (see 3.9).
Asset underperformance as a result of climate change	The Fund has a Responsible Investment policy which sets out its approach to environmental, social and governance risks.

C3. Demographic risks

Demographic Risk	Summary of Control Mechanisms
Pensioners living longer, thus increasing cost to Fund.	Set mortality assumptions with some allowance for future increases in life expectancy. The Fund Actuary has direct access to the experience of over 50 LGPS funds which allows early identification of changes in life expectancy that might in turn affect the assumptions underpinning the valuation.
Maturing Fund – i.e. proportion of actively contributing employees declines relative to retired employees.	Continue to monitor at each valuation, consider seeking monetary amounts rather than % of pay and consider alternative investment strategies.

Demographic Risk	Summary of Control Mechanisms
Deteriorating patterns of early retirements	Employers are charged the extra cost of non ill-health retirements following each individual decision. Employer ill health retirement experience is monitored, and insurance is an option.
Reductions in payroll causing insufficient deficit recovery payments	In many cases this may not be sufficient cause for concern, and will in effect be caught at the next formal valuation. However, there are protections where there is concern, as follows: Employers in the stabilisation mechanism may be brought out of that mechanism to permit appropriate contribution increases (see Note (b) to 3.3). For other employers, review of contributions is permitted in general between valuations (see Note (f) to 3.3) and may require a move in deficit contributions from a percentage of payroll to fixed monetary amounts.

C4. Regulatory risks

Regulatory Risk	Summary of Control Mechanisms
Changes to national pension requirements and/or HMRC rules e.g. changes arising from public sector pensions reform.	The Administering Authority considers all consultation papers issued by the Government and comments where appropriate. The Administering Authority is monitoring the progress on the McCloud court case and will consider an interim valuation or other appropriate action once more information is known. The government's long term preferred solution to GMP indexation and equalisation - conversion of GMPs to scheme benefits - was built into the 2019 valuation.
Time, cost and/or reputational risks associated with any MHCLG intervention triggered by the Section 13 analysis (see Section 5).	Take advice from Fund Actuary on position of Fund as at prior valuation, and consideration of proposed valuation approach relative to anticipated Section 13 analysis.

Regulatory Risk	Summary of Control Mechanisms
Changes by Government to particular employer participation in LGPS Funds, leading to impacts on funding and/or investment strategies.	The Administering Authority considers all consultation papers issued by the Government and comments where appropriate. Take advice from Fund Actuary on impact of changes on the Fund and amend strategy as appropriate.

C5. Governance risks

Governance 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) or not advised of an employer closing to new entrants.	The Administering Authority has a close relationship with employing bodies and communicates required standards e.g. for submission of data. The Actuary may revise the rates and Adjustments certificate to increase an employer's contributions between triennial valuations Deficit contributions may be expressed as monetary amounts.
Actuarial or investment advice is not sought, or is not heeded, or proves to be insufficient in some way	The Administering Authority maintains close contact with its specialist advisers. Advice is delivered via formal meetings involving Elected Members, and recorded appropriately. Actuarial advice is subject to professional requirements such as peer review.
Administering Authority failing to commission the Fund Actuary to carry out a termination valuation for a departing Admission Body.	The Administering Authority requires employers with Best Value contractors to inform it of forthcoming changes. Community Admission Bodies' memberships are monitored and, if active membership decreases, steps will be taken.

Governance Risk	Summary of Control Mechanisms
An employer ceasing to exist with insufficient funding or adequacy of a bond.	The Administering Authority believes that it would normally be too late to address the position if it was left to the time of departure. The risk is mitigated by: Seeking a funding guarantee from another scheme employer, or external body, where-ever possible (see Notes (h) and (j) to 3.3). Alerting the prospective employer to its obligations and encouraging it to take independent actuarial advice. Vetting prospective employers before admission. Where permitted under the regulations requiring a bond to protect the Fund from various risks.
	Requiring new Community Admission Bodies to have a guarantor. Reviewing bond or guarantor arrangements at regular intervals (see Note (f) to 3.3). Reviewing contributions well ahead of cessation if thought appropriate (see Note (a) to 3.3).
An employer ceasing to participate resulting in an exit credit being payable	The Administering Authority regularly monitors admission bodies coming up to cessation. The Administering Authority invests in liquid assets to ensure that exit credits can be paid when required.

Appendix D – The calculation of Employer contributions

In Section 2 there was a broad description of the way in which contribution rates are calculated. This Appendix considers these calculations in much more detail.

As discussed in Section 2, the actuary calculates the required contribution rate for each employer using a three-step process:

- Calculate the funding target for that employer, i.e. the estimated amount of assets it should hold in order to be able to pay all its members' benefits. See Appendix E for more details of what assumptions we make to determine that funding target;

- Determine the time horizon over which the employer should aim to achieve that funding target. See the table in section 3.3 and note (c) for more details;

- Calculate the employer contribution rate such that it has at least a given likelihood of achieving that funding target over that time horizon, allowing for various possible economic outcomes over that time horizon. See the table in section 3.3 and note (e) for more details.

The calculations involve actuarial assumptions about future experience, and these are described in detail in Appendix E.

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

Employer contributions are normally made up of two elements:

a) the estimated cost of ongoing benefits being accrued, referred to as the "Primary rate" (see D2 below); plus

b) an adjustment for the difference between the Primary rate above, and the actual contribution the employer needs to pay, referred to as the "Secondary contribution rate" (see D3 below).

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

D2. How is the Primary rate calculated?

The Primary element of the employer contribution rate is calculated with the aim that these contributions will meet benefit payments in respect of members' **future** service in the Fund. This is based upon the cost (in excess of members' contributions) of the benefits which employee members earn from their service each year.

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

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

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

The projections are carried out using an economic modeller (the "Economic Scenario Service") developed by the Fund's actuary Hymans Robertson: this allows for a wide range of outcomes as regards key factors such as asset returns (based on the Fund's investment strategy), inflation, and bond yields. Further information about this model is included in Appendix E. The measured contributions are calculated such that the proportion of outcomes meeting the employer's funding target (at the end of the time horizon) is equal to the required likelihood.

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

D3. How is the Secondary rate calculated?

The Fund aims for each employer to have assets sufficient to meet 100% of its accrued liabilities at the end of its funding time horizon based on the employer's funding target assumptions (see Appendix E).

The Secondary rate is calculated as the balance over and above the Primary rate, such that the total contribution rate is projected to:

- meet the required funding target relating to combined past and future service benefit accrual, including accrued asset share (see D5 below)
- at the end of the determined time horizon (see 3.3 Note (c) for further details)
- with a sufficiently high likelihood, as set by the Fund's strategy for the category of employer (see 3.3 Note (e) for further details).

The projections are carried out using an economic modeller (the "Economic Scenario Service") developed by the Fund Actuary Hymans Robertson: this allows for a wide range of outcomes as regards key factors such as asset returns (based on the Fund's investment strategy), inflation, and bond yields. Further information about this model is included in Appendix E. The contributions are calculated such that the proportion of outcomes meeting the employer's funding target (by the end of the time horizon) is equal to the required likelihood.

D4. What affects a given employer's valuation results?

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

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

D5. How is each employer's asset share calculated?

The Fund Actuary uses the Hymans Robertson's proprietary "HEAT" system to track employer assets on a monthly basis. Starting with each employer's assets from the previous month end, cash flows paid in/out and investment returns achieved on the Fund's assets over the course of the month are added to calculate an asset value at the month end.

The Fund is satisfied that this new approach provides the most accurate asset allocations between employers that is reasonably possible at present.

D6. How does the Fund adjust employer asset shares when an individual member moves from one employer in the Fund to another?

Under the cash flow approach for tracking employer asset shares, the Fund has allowed for any individual members transferring from one employer in the Fund to another, via the transfer of a sum from the ceding employer's asset share to the receiving employer's asset share. This sum is equal to the member's Cash Equivalent Transfer Value (CETV) as advised by the Fund's administrators.

Appendix E – Actuarial assumptions

E1. What are the actuarial assumptions used to calculate employer contribution rates?

These are expectations of future experience used to place a value on future benefit payments ("the liabilities") and future asset values.

Assumptions are made about the amount of benefit payable to members (the financial assumptions) and the likelihood or timing of payments (the demographic assumptions). For example, financial assumptions include investment returns, salary growth and pension increases; demographic assumptions include life expectancy, probabilities of ill-health early retirement, and proportions of member deaths giving rise to dependants' benefits.

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

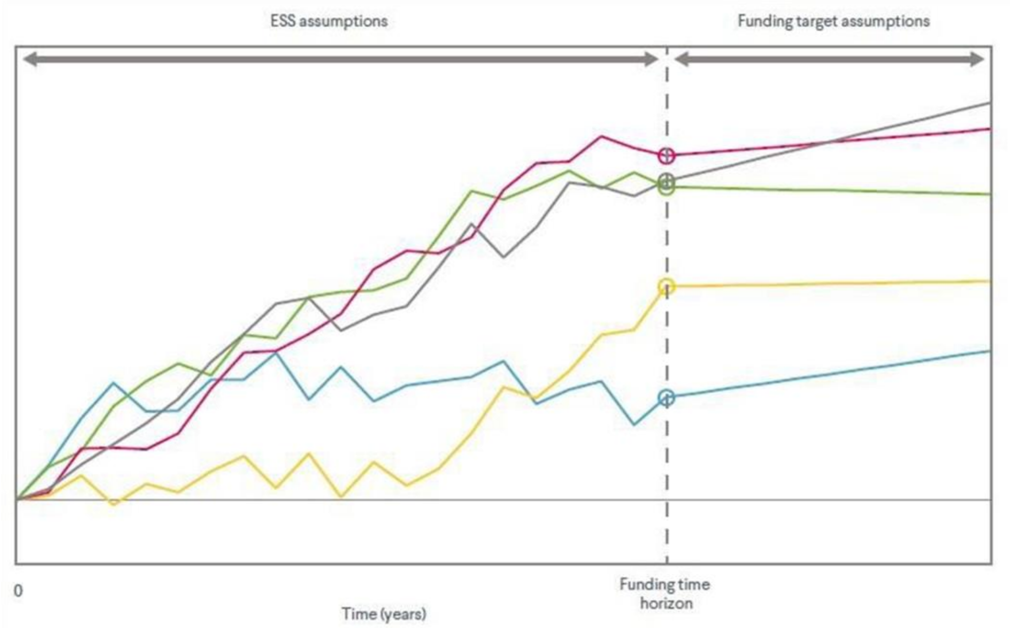
The actuary's approach to calculating employer contribution rates involves the projection of each employer's future benefit payments, contributions and investment returns into the future under 5,000 possible economic scenarios. Future inflation (and therefore benefit payments) and investment returns for each asset class (and therefore employer asset values) are variables in the projections. By projecting the evolution of an employer's assets and benefit payments 5,000 times, a contribution rate can be set that results in a sufficient number of these future projections (determined by the employer's required likelihood) being successful at the end of the employer's time horizon. In this context, a successful contribution rate is one which results in the employer having met its funding target at the end of the time horizon.

Setting employer contribution rates therefore requires two types of assumptions to be made about the future:

1. Assumptions to project the employer's assets, benefits and cash flows to the end of the funding time horizon. For this purpose the actuary uses Hymans Robertson's proprietary stochastic economic model - the Economic Scenario Service ("ESS"). These assumptions vary in two ways: between each of the 5,000 scenarios *and* between each year. Some assumptions might be high in the first few years but then reduce later on (e.g. the blue line in the illustration overleaf) or vice versa (e.g. the yellow line).

2. Assumptions to assess whether, for a given projection, the funding target is satisfied at the end of the time horizon. For this purpose, the Fund has three different funding bases. These assumptions vary between each of the 5,000 scenarios but are fixed from year to year, e.g. one scenario might assume a fixed level of inflation of 5% per year (e.g. the grey or blue lines) whereas another might assume a fixed inflation level of near zero (e.g. the yellow line).

The difference between the two assumptions is represented graphically in the following diagram, where each line represents one of the 5,000 scenarios. Up to the end of the time horizon, the assumptions vary between scenarios *and* from year to year (these are the ESS assumptions). Beyond this point they vary between scenarios but are fixed from year to year (these are the funding target assumptions). The diagram is illustrative so the height of the vertical lines above the axis does not represent any particular variable, but it could be thought of as the cumulative total investment return or inflation, for example.



Details on the ESS assumptions and funding target assumptions are included below (in E2 and E3 respectively).

E2. What assumptions are used in the ESS?

The actuary uses Hymans Robertson's ESS model to project a range of possible outcomes for the future behaviour of asset returns and economic variables.

With this type of modelling, there is no single figure for an assumption about future inflation or investment returns. Instead, there is a range of what future inflation or returns will be which leads to likelihoods of the assumption being higher or lower than a certain value.

The ESS is a complex model to reflect the interactions and correlations between different asset classes and wider economic variables.

The table below shows the calibration of the model as at 31 March 2019. All returns are shown net of fees and are the annualised total returns over 5, 10 and 20 years, except for the yields which refer to the simulated yields at that time horizon.

Economic Scenario Service (ESS)											
	Percentile	Annualised total returns							RPI inflation expectation	17 year real govt bond yield	17 year govt bond yield
		Cash	Index Linked Gilts (medium)	Fixed Interest Gilts (medium)	UK Equity	Overseas Equity	Property	A rated corporate bonds (medium)			
5 years	16th	-0.4%	-2.3%	-2.9%	-4.1%	-4.1%	-3.5%	-2.7%	1.9%	-2.5%	0.8%
	50th	0.7%	0.5%	0.3%	4.0%	4.1%	2.4%	0.8%	3.3%	-1.7%	2.1%
	84th	2.0%	3.3%	3.4%	12.7%	12.5%	8.8%	4.0%	4.9%	-0.8%	3.6%
10 years	16th	-0.2%	-1.8%	-1.3%	-1.5%	-1.4%	-1.5%	-0.9%	1.9%	-2.0%	1.2%
	50th	1.3%	0.0%	0.2%	4.6%	4.7%	3.1%	0.8%	3.3%	-0.8%	2.8%
	84th	2.9%	1.9%	1.7%	10.9%	10.8%	7.8%	2.5%	4.9%	0.4%	4.8%
20 years	16th	0.7%	-1.1%	0.1%	1.2%	1.3%	0.6%	0.7%	2.0%	-0.7%	2.2%
	50th	2.4%	0.3%	1.0%	5.7%	5.8%	4.3%	1.9%	3.2%	0.8%	4.0%
	84th	4.5%	2.0%	2.0%	10.3%	10.4%	8.1%	3.0%	4.7%	2.2%	6.3%
1-yr volatility (Dispersion)		1%	7%	10%	17%	17%	14%	11%	1%		

E3. What assumptions are used in the funding target?

At the end of an employer's funding time horizon, an assessment will be made – for each of the 5,000 projections – of how the assets held compare to the value of assets required to meet the future benefit payments (the funding target). Valuing the cost of future benefits requires the actuary to make assumptions about the following financial factors:

- Benefit increases and Career Average Revalued Earnings (CARE) revaluation
- Salary growth
- Investment returns (the "discount rate")

Each of the 5,000 projections represents a different prevailing economic environment at the end of the funding time horizon and so a single, fixed value for each assumption is unlikely to be appropriate for every projection. For example, a high assumed future investment return (discount rate) would not be prudent in projections with a weak outlook for economic growth. Therefore, instead of using a fixed value for each assumption, the actuary references economic indicators to ensure the assumptions remain appropriate for the prevailing economic environment in each projection. The economic indicators the actuary uses are: future inflation expectations and the prevailing risk free rate of return (the yield on long term UK government bonds is used as a proxy for this rate).

The Fund has three funding bases which will apply to different employers depending on their type. Each funding basis has a different assumption for future investment returns when determining the employer's funding target.

Funding basis	**Ongoing participation basis**	**Contractor exit basis**	**Gilts exit basis**
Employer type	All employers except Transferee Admission Bodies and closed Community Admission Bodies	Transferee Admission Bodies	Community Admission Bodies that are closed to new entrants
Investment return assumption underlying the employer's funding target (at the end of its time horizon)	Long term government bond yields plus an asset outperformance assumption (AOA) of 1.6% p.a.	Long term government bond yields plus an AOA equal to the AOA used to allocate assets to the employer on joining the Fund	Long term government bond yields with no allowance for outperformance on the Fund's assets

E4. What other assumptions apply?

The following assumptions are those of the most significant used in both the projection of the assets, benefits and cash flows and in the funding target.

a) Salary growth

After discussion with Fund officers, the salary increase assumption at the 2019 valuation has been set to be a blended rate combined of:

1. 2.7% in 2019/20 and 2% p.a.. until 31 March 2023, followed by
2. pay increases in line with retail prices index (RPI) inflation thereafter.

This gives a single assumption of RPI less 0.3% p.a., a change from the previous valuation where a blended assumption (constructed in a similar way) of RPI less 0.7% p.a. was used. The change has led to an increase in the funding target (all other things being equal).

b) Pension increases

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

At this valuation, we have continued to assume that CPI is 1.0% p.a. lower than RPI.

c) Life expectancy

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

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

Allowance has been made in the ongoing valuation basis for future improvements in line with the 2018 version of the Continuous Mortality Investigation model published by the Actuarial Profession and a 1.25% per annum minimum underpin to future reductions in mortality rates. This updated allowance for future improvements will generally result in lower life expectancy assumptions and hence a reduced funding target (all other things being equal).

The approach taken is considered reasonable in light of the long term nature of the Fund and the assumed level of security underpinning members’ benefits.

d) General

The same financial assumptions are adopted for most employers (except for the differences in funding basis mentioned in section E3), in deriving the funding target underpinning the Primary and Secondary rates: as described in (3.3), these calculated figures are translated in different ways into employer contributions, depending on the employer's circumstances.

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

Appendix F – Notes to Table 3.3

Note (a) (Basis for CABs and Designating Employers closed to new entrants)

In the circumstances where:

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

The Administering Authority may set a higher funding target (e.g. based on the return from long-term gilt yields and extending the allowance for future improvements in longevity) by the time the agreement terminates or the last active member leaves, in order to protect other employers in the Fund. This policy will increase regular contributions with the objective of reducing, but not entirely eliminating, the possibility of a final deficit payment being required from the employer when a cessation valuation is carried out.

If an employer's contributions are set to target a higher funding target, the Administering Authority may move the employer's assets to a lower risk investment strategy.

The Administering Authority also reserves the right to adopt the above approach in respect of those Designating Employers and Admission Bodies with no guarantor, where the strength of covenant is considered to be weak but there is no immediate expectation that the admission agreement will cease or the Designating Employer alters its designation.

Note (b) (Stabilisation)

Stabilisation is a mechanism where employer contribution rate variations from year to year are kept within a pre-determined range, thus allowing those employers' rates to be relatively stable. This stabilisation mechanism allows short term investment market volatility to be managed so as not to cause volatility in employer contribution rates, on the basis that a long term view can be taken on net cash inflow, investment returns and strength of employer covenant.

The Administering Authority, on the advice of the Fund Actuary, believes that stabilising contributions can still be viewed as a prudent longer-term approach.

However, employers whose contribution rates have been "stabilised" should be aware of the risks of this approach and should consider making additional payments to the Fund if possible.

The current stabilisation mechanism applies if:

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

On the basis of extensive modelling carried out for the 2019 valuation (see Section 4), the contribution rates payable by stabilised employers are subject to maximum annual changes (in either direction) of 1 or 1.5% of pay depending on their circumstances.

All percentage of pay figures are based on the employer's actual payroll and contributions in payment as at 31 March 2019.

The stabilisation criteria and limits apply for the period 1st April 2020 to 31 March 2023 and will be reviewed at the next formal valuation.

The review will take into account the employer's membership profiles, actual payroll and contributions in payment at the time of the review and also any issues surrounding employer security, and other relevant factors. Any material changes to any of the above may result in a revision to the stabilisation criteria and limits

The Administering authority reserves the right to review the stabilisation criteria and limits at any point before 31 March 2022 if there are material events for example (but not limited to) significant reductions in active membership or changes in the nature of the employer (perhaps due to Government restructuring or policy changes).

Note (c) (Maximum time horizon)

The maximum time horizon starts at the commencement of the revised contribution rate (1 April 2020 for the 2019 valuation). The Administering Authority would normally expect the same period to be used at successive valuations, but would reserve the right to propose alternative time horizons, for example where there were no new entrants. This expectation does not apply to contractors.

A maximum time horizon of 20 years is reserved only for employers with tax raising powers or an explicit guarantee from a central government department e.g. DFE guarantee for academies.

For other employers who remain open to active membership the maximum time horizon is 15 years. The maximum time horizon for all contractors is the outstanding contract term
For employers who are closed to new entrants or with no (or very few) active members at this
valuation, the deficit should be recovered by a fixed monetary amount over a period to be agreed with the body or its successor, not to exceed 15 years. Note this period is likely to reduce at each subsequent valuation.

Note (d) (Secondary rate)

In general, the Secondary contribution rate for each employer covering the period until the next valuation will be set as a monetary amount as the default.

Note (e) (Likelihood of success of achieving funding target)

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

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

Different likelihoods are set for different employers depending on their nature and circumstances: in broad terms:

- a 2 in 3 or 66% minimum likelihood is required for employers with tax raising powers or an explicit guarantee from a central government department e.g. DFE guarantee for academies

- a 3 in 4 or 75% minimum likelihood is generally required if the employer does not have tax-raising powers or an explicit guarantee from a central government department e.g. DFE guarantee for academies

- a 2 in 3 or 66% minimum likelihood may be applied for employers who can evidence a tax raising body as a guarantor or other sufficient security backing its funding position

The Fund reserves the right to change or set alternative minimum probabilities if the circumstances of the employer change, for example (but not limited to) the Fund believes the employer poses a greater risk of being unable to meet its long term funding commitment than other employers or the employer is likely to cease participation in the Fund in the short or medium term

Note (f) (Regular Reviews)

Such reviews may be triggered by significant events including but not limited to: significant reductions in payroll, altered employer circumstances, Government restructuring affecting the employer's business, or failure to pay contributions or arrange appropriate security as required by the Administering Authority.

The result of a review may be to require increased contributions (by strengthening the actuarial assumptions adopted and/or moving to monetary levels of deficit recovery contributions), and/or an increased level of security or guarantee.

Note (g) (New Academy conversions)

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

a) The academy will be regarded as a separate employer in its own right and will not be pooled with other employers in the Fund. The only exception is where the academy is part of a Multi Academy Trust (MAT) in which case the academy's figures will be calculated as below but can be combined with those of the other academies in the MAT. The underlying funding position of each academy within the MAT will continue to be tracked.

b) The academy's past service liabilities on conversion will be calculated based on its active Fund members on the day before conversion. For the avoidance of doubt, these liabilities will include all past service of those members, but will exclude the liabilities relating to any ex-employees of the school who have deferred or pensioner status;

c) The academy will be allocated an initial asset share from the ceding council's assets in the Fund. This asset share will be calculated using the estimated funding position of the ceding council at the date of academy conversion. The share will be based on the active members' funding level, having first allocated assets in the council's share to fully fund deferred and pensioner members, subject to a maximum initial academy funding level of 100%. The asset allocation will be based on market conditions and the academy's active Fund membership on the day prior to conversion;

d) The academy's initial contribution rate for the first year ending 31 March from the conversion date will be as per the ceding council's rate. Following the actuarial assessment of the new academy's assets and liabilities, a new, standalone contribution rate will be set which will be payable from 1st April after the conversion date until the next formal valuation. This contribution rate will be assessed using the funding target, time horizon and likelihood of success set out in section 3.3 above;

e) As an alternative to (d), a new academy joining a MAT in which all academies pay the same rate, may pay the MAT rate from the date of joining the MAT. This may not apply if the new academy would significantly alter the membership profile or funding position of the MAT.

f) Ultimately, all academies remain responsible for their own allocated assets and liabilities.

g) It is possible for an academy to leave one MAT and join another. If this occurs, all active, deferred and pensioner members of the academy transfer to the new MAT.

The Fund's policies on academies are subject to change in the light of any amendments to MHCLG and/or DfE guidance or any changes to Government policy, for example if the current provision of a DfE guarantee that the Department will meet any outstanding LGPS liabilities on Academy Trust closure is removed, reduced or becomes insufficient to meet potential risks to the Fund . Any changes will be notified to academies, and will be reflected in a subsequent version of this FSS. In particular, policies (c) and (d) above will be reconsidered at each valuation.

Note (h) (New Admission Bodies)

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

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

Transferee Admission Bodies (TABs): For all TABs, the security must be to the satisfaction of the Administering Authority as well as the letting employer, and will be monitored and reassessed on an annual basis by the Administering Authority. However, it is the responsibility of the letting employer to ensure that the level of security provided remains adequate, as the letting employer is the guarantor of last resort should the TAB default. See also Note (i) below.

Community Admission Bodies (CABs): The Administering Authority will only consider requests from CABs (or other similar bodies, such as section 75 NHS partnerships) to join the Fund if they are sponsored by a Scheduled Body with tax raising powers, guaranteeing their liabilities or provide a form of security as above. The sponsoring Scheduled Body may also require the CAB to provide some form of security, such as a bond.

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

Note (i) (New Transferee Admission Bodies)

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

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

Employers which "outsource" have flexibility in the way that they can deal with the pension risk potentially taken on by the contractor. In particular there are three different routes that such employers may wish to adopt:

i) <u>Pooling</u>
Under this option the contractor is pooled with the letting employer. In this case, the contractor pays the same rate as the letting employer, which may be under a stabilisation approach.

ii) <u>Letting employer retains pre-contract risks</u>
Under this option the letting employer would retain responsibility for assets and liabilities in respect of service accrued prior to the contract commencement date. The contractor would be responsible for the future liabilities that accrue in respect of transferred staff. The contractor's contribution rate could vary from one valuation to the next. It would be liable for any deficit, and entitled to any surplus, at the end of the contract term in respect of assets and liabilities attributable to service accrued during the contract term.

iii) <u>Fixed contribution rate agreed</u>
Under this option the contractor pays a fixed contribution rate throughout its participation in the Fund and on cessation does not pay any deficit or receive an exit credit. In other words, the pension risks 'pass through' to the letting employer.

The Administering Authority requires that a new TAB will participate in the Fund via a fixed contribution rate arrangement with the letting employer. The certified employer contribution rate will be set equal to the fixed contribution rate agreed between the letting authority and the contactor. The fixed rate that will be paid is at the discretion of the letting authority and contractor subject to a minimum rate equal to the letting authority's primary rate when assessed on a probability of achieving funding target of 75% (the funding target and time horizon remain unchanged). Upon cessation the contractor's assets and liabilities will transfer back to the awarding authority with no crystallisation of any deficit or surplus.

In order to avoid the Administering Authority becoming involved in any disputes relating to risk sharing and to protect the other participating employers, the Fund will not be party to any risk sharing agreement between any employer (awarding authority) and a contractor. Accordingly any such arrangements will not be detailed in the admission agreement and the admission body will be required to follow the principles of the agreement as if no such risk sharing was in place and as if they were any other employer within the Cheshire Pension Fund. It is at the sole discretion of the Administering Authority as to whether any risk sharing agreement is recognised in the certified employer contribution rate. If the risk arrangement is not recognised, then it will then be up to the awarding authority and the contractor to put in place separate steps to allow the risk sharing to be implemented (e.g. via the contract payments). Accordingly the contractor will be required to pay the certified employer contribution rate to the Fund and any other contributions required e.g. early retirement strain costs, regardless of risk sharing arrangement in place.

Any risk-sharing agreement should ensure that some element of risk transfers to the contractor where it relates to their decisions and it is unfair to burden the lettering employer with that risk. For example, the contractor should typically be responsible for pension costs that arise from:

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

Note (j) (Admission Bodies Ceasing)

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

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

- The insolvency, winding up or liquidation of the Admission Body;

- Any breach by the Admission Body of any of its obligations under the Agreement that they have failed to remedy to the satisfaction of the Fund;

- A failure by the Admission Body to pay any sums due to the Fund within the period required by the Fund; or

- The failure by the Admission Body to renew or adjust the level of the bond or indemnity, or to confirm an appropriate alternative guarantor, as required by the Fund.

On cessation, the Administering Authority will instruct the Fund actuary to carry out a cessation valuation to determine whether there is any deficit or surplus. Where there is a deficit, payment of this amount in full would normally be sought from the Admission Body, where there is a surplus, an exit credit may be paid to the Admission Body in line with the Administering Authority's exit credit policy. (see Appendix H)

As discussed in section 2.7, the LGPS benefit structure from 1 April 2014 is currently under review following the Government's loss of the right to appeal the McCloud and other similar court cases. The Fund has considered how it will reflect the current uncertainty regarding the outcome of this judgement in its approach to cessation valuations. For cessation valuations that are carried out before any changes to the LGPS benefit structure (from 1 April 2014) are confirmed, the actuary may make an adjustment to the ceasing liability value depending on the employer's circumstances.

The Fund Actuary charges a fee for carrying out an employer's cessation valuation, and there will be other Fund administration expenses associated with the cessation, both of which the Fund will recharge to the employer. For the purposes of the cessation valuation, this fee will be treated as an expense incurred by the employer and will be deducted from the employer's exit credit or added to the employer's cessation deficit, as appropriate. This process improves administrative efficiency as it reduces the number of transactions required to be made between the employer and the Fund following an employer's cessation.

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

- Where a guarantor does not exist then, in order to protect other employers in the Fund, the cessation liabilities and final surplus/deficit will normally be calculated using a "gilts exit basis", which is more prudent than the ongoing participation basis. This has no allowance for potential future investment outperformance above gilt yields, and has added allowance for future improvements in life expectancy. This could give rise to a significant cessation payment being required.

- Where there is a guarantor for future deficits and contributions, the details of the guarantee will be considered prior to the cessation valuation being carried out. In some cases the guarantor is simply guarantor of last resort and therefore the cessation valuation will be carried out consistently with the approach taken had there been no guarantor in place. Alternatively, where the guarantor is not simply guarantor of last resort, the cessation may be calculated using the ongoing participation basis or contractor exit basis as described in Appendix E;

- Again, depending on the nature of the guarantee, it may be possible to simply transfer the former Admission Body's liabilities and assets to the guarantor, without needing to crystallise any deficit or surplus. This approach may be adopted where the employer cannot pay the contributions due.
  This will be considered on a case by case basis subject to approval by the guarantor and is within the terms of the guarantee;

Under (a) and (b), any shortfall would usually be levied on the departing Admission Body as a single lump sum payment. If this is not possible then the Fund, at its absolute discretion may allow spreading the payment over a period acceptable to the Fund. This will be considered on case by case basis and the Fund may require some security in place for the employer such as a bond indemnity or guarantee.

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

As an alternative, where the ceasing Admission Body is continuing in business, the Fund at its absolute discretion reserves the right to enter into an agreement with the ceasing Admission Body. Under this agreement the Fund would accept an appropriate alternative security to be held against any deficit on the gilts exit basis, and would carry out the cessation valuation on the ongoing participation basis. Secondary contributions would be derived from this cessation debt.

This approach would be monitored as part of each triennial formal valuation and secondary contributions would be reassessed as required. The Admission Body may terminate the agreement only via payment of the outstanding debt assessed on the gilts exit basis. Furthermore, the Fund reserves the right to revert to the "gilts exit basis" and seek immediate payment of any funding shortfall identified. The Administering Authority may need to seek legal advice in such cases, as the Admission Body would have no contributing members.

Exit Credits

If an employer becomes an exiting employer under Regulation 64 of the 2013 LGPS Regulations (as amended), it may be entitled to receive an exit credit.

The administering authority may determine, at its absolute discretion, the amount of any exit credit payment due (which may be zero), having regard to any relevant considerations.

The relevant considerations that the administering authority must consider are:

- The extent to which the employer's assets are in excess of its liabilities
- The proportion of the excess of assets which has arisen because of the value of employer's contributions
- Any representations made by the exiting employer and its letting authority/guarantor
- Any other relevant factors.

The Administering Authority's exit credit policy is published at Appendix H of this FSS.

Appendix G – Glossary

Term	Meaning
Active Member	A current employee paying into the Fund
Administering Authority	The council with statutory responsibility for running the Fund
Admission Bodies	Employers where there is an Admission Agreement setting out the employer's obligations and which employees are nominated to participate in the Fund. These can be Community Admission Bodies or Transferee Admission Bodies. For more details (see 2.3).
Covenant	The assessed financial strength of the employer. A strong covenant indicates a greater ability to pay for pension obligations in the long run. A weaker covenant means that it appears that the employer may have difficulties meeting its pension obligations in full over the longer term.
Designating Employer	Employers such as town and parish councils that are able to participate in the LGPS via resolution. These employers can designate which of their employees are eligible to join the Fund.
Employer	An individual participating body in the Fund, which employs (or used to employ) **members** of the Fund. Normally the assets and **funding target** values for each employer are individually tracked, together with its **Primary rate** at each **valuation**.
Funding basis	The combined set of assumptions made by the actuary, regarding the future, to calculate the value of the funding target at the end of the employer's time horizon. The main assumptions will relate to the level of future investment returns, salary growth, pension increases and longevity. More prudent assumptions will give a higher funding target, whereas more optimistic assumptions will give a lower funding target.
Gilt	A UK Government bond, i.e. a promise by the Government to pay interest and capital as per the terms of that particular gilt, in return for an initial payment of capital by the purchaser. Gilts can be "fixed interest", where the interest payments are level throughout the gilt's term, or "index-linked" where the interest payments vary each year in line with a specified index (usually RPI). Gilts can be bought as assets by the Fund, but are also used in funding as an objective measure of a risk-free rate of return.
Guarantee / guarantor	A formal promise by a third party (the guarantor) that it will meet any pension obligations not met by a specified employer. The presence of a guarantor will mean, for instance, that the Fund can consider the employer's **covenant** to be as strong as its guarantor's.

Term	Meaning
Letting employer	An employer which outsources or transfers a part of its services and workforce to another employer (usually a contractor). The contractor will pay towards the LGPS benefits accrued by the transferring members, but ultimately the obligation to pay for these benefits will revert to the letting employer. A letting employer will usually be a local authority, but can sometimes be another type of employer such as an Academy.
LGPS	The Local Government Pension Scheme, a public sector pension arrangement put in place via Government Regulations, for workers in local government. These Regulations also dictate eligibility (particularly for Scheduled Bodies), members' contribution rates, benefit calculations and certain governance requirements. The LGPS is divided into 100 Funds which map the UK. Each LGPS Fund is autonomous to the extent not dictated by Regulations, e.g. regarding investment strategy, employer contributions and choice of advisers.
Major Employing Bodies	Tax raising and precepting bodies such as Councils, Police and Fire Authorities and Town & Parish Council
Maturity	A general term to describe a Fund (or an employer's position within a Fund) where the members are closer to retirement (or more of them already retired) and the investment time horizon is shorter. This has implications for investment strategy and, consequently, funding strategy.
Members	The individuals who have built up (and may still be building up) entitlement in the Fund. They are divided into actives (current employee members), deferreds (ex- employees who have not yet retired) and pensioners (ex-employees who have now retired, and dependants of deceased ex-employees).
Primary rate	The employer contribution rate required to pay for ongoing accrual of active members' benefits (including an allowance for administrative expenses). See Appendix D for further details.
Profile	The profile of an employer's membership or liability reflects various measurements of that employer's **members**, i.e. current and former employees. This includes: the proportions which are active, deferred or pensioner; the average ages of each category; the varying salary or pension levels; the lengths of service of active members vs their salary levels, etc. A membership (or liability) profile might be measured for its **maturity** also.
Rates and Adjustments Certificate	A formal document required by the LGPS Regulations, which must be updated at the conclusion of the formal **valuation**. This is completed by the actuary and confirms the contributions to be paid by each employer (or pool of employers) in the Fund for the period until the next valuation is completed.

Term	Meaning
Scheduled Bodies	Types of employer explicitly defined in the LGPS Regulations, whose employers must be offered membership of their local LGPS Fund. These include Councils, colleges, universities, academies, police and fire authorities etc, other than employees who have entitlement to a different public sector pension scheme (e.g. teachers, police and fire officers, university lecturers).
Secondary rate	The difference between the employer's actual and **Primary rates**. See Appendix D for further details.
Stabilisation	Any method used to smooth out changes in employer contributions from one year to the next. This is very broadly required by the LGPS Regulations, but in practice is particularly employed for large stable employers in the Fund.
Valuation	A risk management exercise to review the **Primary** and **Secondary contribution rates**, and other statutory information for a fund, and usually individual employers too. This is normally carried out in full every three years (although this may change in future), but can be approximately updated at other times. The assets value is based on market values at the valuation date, and the liabilities value and contribution rates are based on long term bond market yields at that date also.

Appendix H – Exit Credit Policy

Introduction

The Local Government Pension Scheme (Amendment) Regulations 2020 came into force on 20 March 2020, and are effective from 14 May 2018.

If an employer becomes an exiting employer on or after 14 May 2018 under Regulation 64 of the 2013 Local Government Pension Scheme (LGPS) Regulations (as amended) it may be entitled to receive an exit credit.

In accordance with Regulation 64(2ZAB) of the LGPS Regulations 2013, the Administering Authority will determine the amount of any exit credit (which may be zero) by taking into account the factors set out in Regulation 64(2ZC):

a. the extent to which there is an excess of assets in the fund relating to that employer over the liabilities specified in paragraph (2)(a);
b. the proportion of this excess of assets which has arisen because of the value of the employer's contributions;
c. any representations to the administering authority made by the exiting employer and, where that employer participates in the scheme by virtue of an admission agreement, any body listed in paragraphs (8)(a) to (d)(iii) of Part 3 to Schedule 2 to these Regulations; and
d. any other relevant factors

Cheshire Pension Fund Policy

In determining whether an exit credit may be payable, Cheshire West & Chester Council as Administering Authority for the Cheshire Pension Fund will apply the following principles.

1. If an employer becomes an exiting employer on or after 14 May 2018 under Regulation 64 of the 2013 Local Government Pension Scheme (LGPS) Regulations (as amended) it may be entitled to receive an exit credit.

2. In order to protect other employers, liabilities to determine the amount of any exit credit will be calculated on a "gilts exit basis"

3. Employers within a funding pool (e.g. the Town and Parish Councils pool or a multiacademy trust with more than one school in the Fund) will not normally receive exit credits upon leaving the Fund provided the remaining participants of the pool take responsibility for the residual assets and liabilities after the employer has exited.

4. No exit credit will be payable to any employer who participates in the Fund via the mandated pass through approach as set out in the Funding Strategy Statement.

5. If an employer becomes an exiting employer under Regulation 64 of the 2013 LGPS Regulations (as amended) and an exit payment is payable to the Fund over such period of time as the administering authority considers reasonable, no exit credit will be payable at any future date in relation to that specific agreement as a participating employer.

6. The Administering Authority may calculate an exit credit payment which reflects any contractual pension risk sharing provisions between the exiting employer and the letting authority and/or other relevant scheme employer. This information, which will include which party is responsible for which funding risk, must be presented in writing to the Administering Authority and in clear terms. The document must be agreed by the exiting employer and the letting authority and/or other relevant scheme employer, and presented to the Administering Authority no later than one month after the exiting employer ceases participation in the Fund. Where a variation to the original letting contract is required to facilitate any agreement containing the required information, this will be agreed between the exiting employer and the letting authority and/or other relevant scheme employer.

7. Where a guarantor arrangement is in place, but no formal pension risk-sharing arrangement exists, the Administering Authority may consider any representations as to how the approach to setting contribution rates, payable by the exiting employer during its participation in the Fund, reflects which party is responsible for funding risks. This may inform the determination of the value of any exit credit payment.

8. The Administering Authority will consider any representations made by the letting authority and/or other relevant scheme employer regarding monies owed to them by the exiting employer in respect of the contract/services under which the exiting employer participates in the Cheshire Pension Fund. These representations must be made in writing to the Administering Authority in clear terms no later than one month after the exiting employer ceases participation in the Fund. Where a variation to the original letting contract is required to facilitate any agreement containing the required information, this will be agreed between the exiting employer and the letting authority and/or other relevant scheme employer.

9. If there is any dispute from either party with regards interpretation of contractual, risk sharing or guarantor agreements as outlined above, the Administering Authority will withhold payment of any exit credit until such disputes are resolved by the letting authority and/or other relevant scheme employer and the exiting employer.

10. The Administering Authority will advise the exiting employer as well as the letting authority and/or other relevant scheme employers of its exit credit determination under Regulation 64.

11. The Administering Authority will take into account whether any contributions due or monies owed to the Fund remain unpaid by the exiting employer at the cessation date. If contributions or monies are due to the Fund, the Administering Authority will notify these to the exiting employer and will deduct these from any exit credit payment.

12. The Administering Authority's final decision will be made by the Pension Fund Manager in the first instance, in conjunction with advice from the Fund's Actuary, and/or legal advisors and Chief Operating Officer where necessary, in consideration of the points held within this policy. Where any dispute remains unresolved, the parties will use the internal dispute resolution procedure specified in MHCLG guidance and Regulations.

13. The Administering Authority accepts that there may be some situations that are bespoke

in nature and do not fall into any of the categories set out above. In these situations the decision of the Administering Authority is final in interpreting how any arrangement applies to the value of an exit credit payment.

14. The Administering Authority will advise the exiting employer of the exit credit amount due to be repaid and seek to make the payment within six months of the exit date. In order to meet the six-month timeframe, the Fund requires prompt notification of an employer’s exit and for all data and relevant information to be provided as requested. The Administering Authority is unable to make any exit credit determination or payment until it has received all data and information required and if the delay caused by the Fund requiring data means the 6 month date is passed, the parties will work constructively to enable the Administering Authority to reach its decision as soon as possible thereafter