Agenda Item 6

Funding Strategy Statement

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FALKIRK COUNCIL

Subject: **Funding Strategy Statement**

Meeting: **Joint Meeting of Pensions Committee and Pension Board**

Date: **18 March 2021**

Submitted by: **Director of Corporate and Housing Services**

1. Purpose of Report

1.1 This report seeks the approval of the Pensions Committee for the finalised version of the Funding Strategy Statement (FSS). This follows the circulation of the draft FSS to stakeholders for comment at the end of last year.

2. Recommendations

2.1 The Pensions Committee and Pension Board are asked to note the updated version of the Funding Strategy Statement; and

2.2 The Pensions Committee is asked to approve the Funding Strategy Statement.

3. Background

3.1 As reported at the September Joint Meeting, the Local Government Pension Scheme requires all administering authorities to prepare, maintain and publish a Funding Strategy Statement ("FSS").

3.2 The FSS is the formal record of how the Fund will fund its liabilities. It is the framework within which the Fund's actuary carries out triennial valuations to set employer contribution rates. The FSS requires to be agreed prior to the formal Valuation Report being signed off by the actuary.

3.3 The FSS is required to explain how the Fund will seek to ensure that:

- employers' liabilities are met;
- a prudent long-term approach is taken to funding the liabilities;

- employer contributions rates are as stable as possible; and
- rates are set having regard to inter-generational fairness.

3.4 It is recognised that key objectives, such as securing fund solvency whilst simultaneously maintaining stable and affordable contribution rates, may be contradictory and it is a function of the FSS to balance these conflicting aims.

3.5 The FSS aims to provide transparency around the Fund's funding objectives and give employers' reassurance that their individual funding positions are being determined in a fair and consistent manner.

4. The Funding Strategy Statement for the 2020 Valuation

4.1 A draft FSS for the Falkirk Fund was presented to the joint meeting in September 2020.

4.2 The FSS explains in detail how the actuary will determine individual employer contribution rates and how these may be affected by the characteristics of the employer in question (e.g. scheduled or admission body; open or closed to new members; contractor or charitable body; guarantor or no guarantor, etc). In broad terms, the actuary will set the employer contribution rates taking account of the following three components:

1. the **funding target** – this is the amount of money that each employer will need to hold in order to pay benefits as they fall due
2. the **time horizon** – this is the time period over which the employer will be scheduled to reach the funding target
3. the **likelihood of success** – this is the degree of certainty that the Fund wishes to have in relation to the funding target being achieved, taking account of the time horizon, any particular employer characteristics, and the variety of economic scenarios that could play out during the journey towards the funding target.

4.3 As noted in the September papers the overall strategy for the Fund is for it to be fully funded in the long term with most Fund employers having a 20 year time horizon in which to target this. In practice, progress towards full funding will be reviewed at successive future valuations.

4.4 In accordance with statutory requirements, the draft FSS has been circulated to all Fund employers and Trades Unions for comment.

4.4 The sole response to the consultation was from Police Scotland who sought to clarify a couple of points relating to Cost Cap and Goodwin however no update was required to the FSS as a result of this response.

4.5 Following completion of the valuation process and meetings with employers the following updates have been made to the draft FSS for clarity –

- some revised wording as to how the allowance for cost cap uncertainty has been built into the contribution rates (page 8 of FSS) –
    - Stabilised employers – 0.5% added to rates in the last year 2023/24
    - Non- stabilised employers – no significant change to benefits/costs assumed when setting contributions but the Fund is reserving the right to review contributions following the publication of the Cost Cap valuation
- details of the employers in each employer type have been added for transparency (pages 14 and 15 of FSS)

4.6 The updated FSS has been reviewed to the satisfaction of Hymans Robertson, the Fund Actuary and the finalised version is attached In Appendix 1.

5. Implications

Financial

5.1 The FSS is the framework within which the actuary sets employer contribution rates. Payment of contributions at an appropriate level is a key factor - along with investment returns – in maintaining fund solvency.

Resources

5.2 None.

Legal

5.3 There is a statutory requirement for the Fund to maintain a FSS.

Risk

5.4 Failure to have a relevant FSS could lead to uncertainty around funding aims and a lack of consistency in the way the Fund approaches its funding issues.

Equalities

5.5 None.

Sustainability/Environmental Impact

5.6 None.

6. Conclusion

6.1 The Funding Strategy Statement (FSS) has been consulted upon and some small updates incorporated into a finalised version. This has been reviewed by the Actuary.

6.2. Subject to the FSS being approved, it will be publicised and made available to Fund stakeholders via the Fund website.

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Appendices

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Falkirk Council Pension Fund

Funding Strategy Statement

March 2021

PUBLIC SECTOR

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1 Introduction

1.1 What is this document?

This is the Funding Strategy Statement (FSS) of the Falkirk Council Pension Fund ("the Fund"), which is administered by Falkirk 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 trades unions. It is effective from **Date to be completed**.

1.2 What is the Falkirk Council Pension Fund?

The Fund is part of the Scottish 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 country. The Administering Authority runs the Falkirk Council Pension Fund, in effect the LGPS for the Central Scotland area, to make sure it:

- 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 Fund benefits to the members (as and when they retire, for the rest of their lives), and to their dependants (as and when members die), as defined in the various LGPS Regulations applicable to Scotland. 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 the market values of investments or the level of employer contributions. Investment returns will help pay for some of the benefits, but probably not all, and certainly with no guarantee. Employees' contributions are fixed in the Regulations at a level which only partially covers the cost of the benefits.

Employers therefore need to pay the balance of the cost of benefits to members and their dependants.

The FSS focuses on how employer liabilities are measured, the pace at which these liabilities are funded, and how employers or pools of employers 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,
- prudence in the funding basis, and
- ensuring costs are not deferred to the future.

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

The FSS is a summary of the Fund's approach to funding its liabilities~~,~~ and includes reference to some of the Fund's other policies; it is not an exhaustive statement of policy on all issues. The FSS forms part of a framework which includes:

- the LGPS Regulations applicable in Scotland;
- the Rates and Adjustments Certificate (confirming employer contribution rates for the next three years) which can be found in an appendix to the formal valuation report;
- actuarial factors for valuing individual transfers, early retirement costs and the costs of buying added service; and
- the Fund's Statement of Investment Principles (see Section 4)

1.4 How does the Fund and this FSS affect me?

This depends on 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 employer that 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 future. Note that the FSS applies to all employers participating in the Fund;
- an Elected Member 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: you will want to know how your Council seeks to strike the balance above, such that contributions to the pension fund are being managed in an efficient and effective manner enabling the bulk of council expenditure to focus on service provision and minimising cross-subsidies between different generations of tax-payers.

1.5 What does the FSS aim to 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'/dependants' benefits as they fall due for payment;
- to ensure that employer contribution rates are reasonably stable, 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. a glossary explaining the technical terms occasionally used here.

If you have any other queries please contact Falkirk Council Pension Fund in the first instance at:

Pensions Section or pensions@falkirk.gov.uk
PO Box 14882
Falkirk Council
Municipal Buildings
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2 Basic Funding issues

(More detailed and extensive descriptions are given in Appendix D).

2.1 Key funding objective

The key funding objectives are:

- To ensure that the Fund has a sufficiently high likelihood of holding assets to meet future benefits over the long term;
- To maintain stable contributions insofar as is possible while continuing to protect the long-term solvency of the Fund; and
- To have cash available to pay member's benefits when they are due.

2.2 How does the actuary calculate the required contribution rate?

In essence this is a three-step process:

1. Calculate the funding target for that employer, i.e. the estimated amount of assets it should hold in monetary terms 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;

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;

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.

2.3 What is each employer's contribution rate?

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

a) the estimated cost of benefits being built up each year, after deducting the members' own contributions and including an allowance for administration expenses. This is referred to as the "*Primary rate*", and is expressed as a percentage of members' pensionable pay; 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 rate*". In broad terms, this is in respect of benefits already accrued at the valuation date. The Secondary rate may be expressed as a percentage of pay and/or a monetary amount in each year.

The 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 minima, with employers able to pay contributions at a higher rate. Account of any higher rate contributions will be taken by the Fund actuary at subsequent valuations, i.e. will be reflected as a credit when next calculating the employer's contributions.

2.4 What different types of employer 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.

In essence, participation in the LGPS is open to public sector employers providing some form of service to the local community. Whilst the majority of members will be local authority employees (and ex-employees), the majority of participating employers are those providing services in place of (or alongside) local authority services: colleges, contractors, housing associations, charities, etc.

The LGPS Regulations define various types of employer as follows:

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

Other employers are able to participate in the Fund via an admission agreement, and are referred to as 'admission bodies'. These employers are generally those with a "community of interest" with another scheme employer – **community admission bodies** ("CAB") or those providing a service on behalf of a scheme employer – **transferee admission bodies** ("TAB"). CABs will include housing associations and charities, TABs will generally be contractors. The Fund is able to set its criteria for participation by these employers and can refuse entry if the requirements as set out in the Fund's admissions policy are not met. (NB The terminology CAB and TAB has been dropped from the LGPS Regulations, which instead combine both under the single term 'admission bodies'; however, we have retained the old terminology here as we consider it to be helpful in setting funding strategies for these different employers).

2.5 How does the calculated contribution rate vary for different employers?

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

1. 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;

2. The **time horizon** required is, in broad terms, the period over which the funding target is achieved. Employers may be given a shorter time horizon if they have a less permanent anticipated membership, or do not have income arising from tax-raising powers or statutory fees to cover the cost of increased contributions if investment returns under-perform; and

3. The **likelihood 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 3.4.

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.

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2.6 How is a funding level calculated?

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

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

If this 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 shortfall 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. Whilst we recognise that various parties will take an interest in these measures, for most employers the key issue is how likely it is that their contributions will be sufficient to pay for their members' benefits (when added to their existing asset share and anticipated investment returns).

In short, deficits and funding levels are short term measures, whereas contribution-setting is a longer term issue.

2.7 How does the Fund recognise that contribution levels can affect council and employer service provision, and council tax?

The Administering Authority and the Fund actuary are acutely aware that, all other things being equal, a higher contribution required to be paid to the Fund will mean less cash available for the employer to spend on the provision of services. For instance:

- Higher pension fund contributions may result in reduced council spending, which in turn could affect the resources available for council services, and/or greater pressure on council tax levels;
- Contributions which colleges and universities pay to the Fund will therefore not be available to pay for providing education; and
- Other employers will provide various services to the local community, perhaps through housing, charitable work, or contracting council services. If they are required to pay more in pension contributions to the LGPS then this may affect their ability to provide the local services.

It should be borne in mind that:

- The Fund provides invaluable financial security to families, whether to those who formerly worked in the service of the community who have now retired, or to their families after their death;
- The Fund must have the assets available to meet these retirement and death benefits, which in turn means that the various employers must each pay their own way. Lower contributions today may 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 employees 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;
- The Fund wishes to avoid the situation where an employer falls behind in managing its funding shortfall such that its deficit becomes unmanageable in practice.
- The Fund wishes to avoid employer insolvency and the risk of any resulting deficit falling on the other Fund employers. In that situation, those employers' services would in turn suffer as a result; and
- Employer contributions to the Fund should be at a suitable level, to protect the interests of different generations. For instance, underpayment of contributions for some years will need to be balanced by overpayment in other years; the Fund will wish to minimise the extent to which service recipients in one period are in effect benefitting at the expense of those in a different period.

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 increases to various degrees (see 3.1). In deciding which of these techniques to apply to any given employer, the Fund takes a view on the financial standing of the employer, i.e. its ability to meet its funding commitments over the relevant time horizon.

The Fund will risk assess employers using a knowledge base that 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, any guarantors or security provision, material changes anticipated, etc.

Where the Fund has reasonable confidence that an employer will be able to meet its funding commitments, the Fund will permit options such as stabilisation (See 3.3 Note (b)) over a longer time horizon relative to other employers, and/or a lower likelihood of achieving their funding target. Such options will temporarily produce lower contribution levels than would otherwise have applied. 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 an employer will be able to meet its funding commitments or withstand a significant change in its commitments, then a higher funding target, and/or a time horizon relative to other employers, and/or a higher likelihood of achieving the target may be required.

The Fund actively engages with its employers to agree appropriate contribution levels: see Appendix A.

2.8 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 LGPS benefit structure is currently under review following the Government's loss of the right to appeal two Court of Appeal judgements in December 2018, collectively referred to as the 'McCloud' judgement. 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 2015 in the case of the LGPS in Scotland) were unlawful on the grounds of age discrimination. The exact details of the solution to the McCloud judgement have yet to be confirmed. A consultation on this closed on 23 October 2020 and is currently under consideration by the Scottish Public Pensions Agency (SPPA).

In May 2020, the SPPA set out their expectations for how funds should allow for this uncertainty in the benefit structure as part of their 2020 valuations. The Fund Actuary has included an allowance in the Fund's liabilities in line with SPPA's instructions.

2.9 What approach has the Fund taken to dealing with uncertainty arising from the paused Cost Cap mechanism and its potential impact on the LGPS benefit structure?

As part of the public sector pension scheme reforms in the first half of the 2010s, a mechanism was put in place to protect employers from significant increases in future pension costs. The mechanism is symmetrical in its design – following a Cost Cap valuation carried out by the Government Actuary's Department (GAD), if the scheme is calculated to have a lower/(higher) than intended cost to employers, then action will be taken: improvements/(reductions) in future benefit accrual and/or increases/(reductions) in employee contribution rates.

The first Cost Cap mechanism for LGPS Scotland was as at 31 March 2017, however this has been put on hold until the McCloud judgement is resolved. There is currently no information available about the results of the 2017 Cost Cap valuation and whether a change in the benefit structure and/or employee contribution rates from 1 April 2020 may occur.

The Fund has considered how it will allow for this uncertainty in the approach to setting employer contribution rates:

- For employers where contribution rates are stabilised, a contribution rate increase of 0.5% of pay will be certified for 2023/24.
- Contributions rates for non-stabilised employers will be set assuming no significant benefit increases. However the Fund reserves the right to review contribution rates following the publication of the results of the Cost Cap valuation.

2.10 What approach has the Fund taken to dealing with uncertainty arising from the Goodwin case

The impact of the Goodwin case on Fund liabilities is expected to be small, and will largely be an administrative concern. In the absence of a resolution to this case or any guidance, no allowance has been made for this within the 2020 formal valuation.

2.11 When will the next actuarial valuation be?

On 21 January 2020 SPPA issued a consultation seeking views on proposals to amend the LGPS valuation cycle in Scotland from a three year (triennial) valuation cycle to a four year (quadrennial) valuation cycle. This consultation closed on 9 March 2020 and is currently under consideration by SPPA.

In the absence of any update on this consultation prior to the agreement of the Rates and Adjustments Certificate, the Fund will assume that the next valuation will happen on 31 March 2023 and reserves the right to review contributions if the intervaluation period is extended.

3 Calculating contributions for individual Employers

3.1 General comments

A key challenge for the Fund is to balance the need for stable, affordable employer contributions with the requirement to take a prudent, longer-term view of funding and ensure the solvency of the Fund. 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 is required to reach that funding target? This will always be less than 100% as we cannot be certain of the future. Higher likelihood "bars" 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 Fund 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 FSS. Therefore the Fund 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 Fund may permit employers to pay contributions at a lower level than is assessed for the employer using the three step process in 3.1 above. At their absolute discretion the Fund may:

- extend the time horizon for targeting full funding;
- adjust the required likelihood 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 will result in a lower level of future investment returns on the employer's asset share. Thus, deferring a certain amount of contribution 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 (3.3) is a summary of how the main funding policies differ for different types of employer, followed by more detailed notes where necessary.

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

3.3 The different approaches used for different employers

Type of employer	Scheduled Bodies		Community Admission Bodies		Transferee Admission Bodies
Sub-type	**Local Authorities and similar employers** Note (a)	**Police, Fire and other eligible employers** Note (b)	**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 participation basis, but may move to "low risk exit basis" - see Note (c)		Contractor exit basis, assumes fixed contract term in the Fund (see Appendix E)
Pooling	For contribution rate setting only (individual asset shares are tracked)	No pooling	Where appropriate, pooled contribution rates for employers with fewer than 30 members at the valuation date (see 3.4)		No pooling
Primary rate approach	(see Appendix D – D.2)				
Stabilised contribution rate?	Yes - see Note (d)		No	No	No
Maximum time horizon – Note (e)	20 years	20 years	Up to 20 years	Up to the future working lifetime of the remaining active membership	Shorter of outstanding contract term and future working lifetime
Secondary rate – Note (f)	Monetary amount (unless otherwise agreed)				
Secondary rate calculations when funding level is greater than 100% at valuation date	Covered by stabilisation arrangement		Preferred approach: contributions kept at Primary rate. However, reductions may be permitted by the Fund		Permit contribution rate reductions if calculated secondary rate is negative
Likelihood of achieving target – Note (g)	70%	70%	70% (or 50% if funding target is low risk exit basis)	70% (or 50% if funding target is low risk exit basis)	60%
Phasing of contribution changes	Covered by stabilisation arrangement		3 years	3 years	None
Review of rates – Note (h)	The Fund reserves the right to review contribution rates and amounts, and the level of security provided, at regular intervals between valuations.				
New employer	n/a		Note (i)		Notes (i) & (j)
Cessation of participation: exit debt/credit payable	Cessation is assumed not to be generally possible, as Scheduled Bodies are legally obliged to participate in the LGPS. In the event of cessation occurring (e.g. machinery of Government changes), the cessation debt		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 (k).		Participation is assumed to expire at the end of the contract. Exit debt/credit (if any) calculated using a basis consistent with

	principles applied would be as per Note (k).		that used to allocate assets on joining the Fund, unless the Admission Agreement is terminated early. In that circumstance a more prudent basis would apply. The Letting Authority will be liable for future deficits and contributions arising see Note (k).

Note (a) ('The Local Government Group' of employers)

- Clackmannanshire Council
- Falkirk Council
- Stirling Council
- Central Scotland Joint Valuation Board

Note (b) (Other employers with stabilised rates)

- Scottish Fire and Rescue Service
- Scottish Police Authority
- Strathcarron Hospice
- Forth Valley College
- Scottish Environment Protection Agency
- Scottish Children's Reporter Administration

Note (c) (Basis for CABs closed to new entrants)

In the circumstances where:

- the employer is an Admission Body but not a Transferee Admission Body, and
- the employer has no guarantor, and
- the admission body is closed to future new entrants (either explicitly, or implicitly due to a lack of employees joining the Fund in recent times)

The Fund may set a higher funding target (e.g. the "low risk exit basis" as per E2) in order to protect other employers in the Fund. This policy will increase regular contributions and reduce, but not entirely eliminate, the possibility of a final deficit payment being required from the employer when a cessation valuation is carried out.

The Fund also reserves the right to adopt the above approach in respect of those 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.

Note (d) (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. In the interests of stability and affordability of employer contributions, the Fund, 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" (and may therefore be paying less than their theoretical contribution rate) should be aware of the risks of this approach and should consider making additional payments to the Fund if possible.

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 current stabilisation mechanism applies if:

- the employer satisfies the eligibility criteria set by the Fund (broadly that the employer is open and has a very high covenant e.g. a tax-raising body) and;
- there are no material events which cause the employer to become ineligible, e.g. significant reductions in active membership (due to outsourcing or redundancies), or changes in the nature of the employer (perhaps due to Government restructuring), or changes in the security of the employer, or the provision of poor membership data from an employer leading to uncertainty about their level of liabilities.

For the period from 1 April 2021 to 31 March 2024, the stabilised mechanism will be a maximum increase of 0.5% of pay p.a. and a maximum decrease of 0.5% of pay p.a. applies.

The stabilisation criteria and limits will be reviewed prior to the 31 March 2023 valuation, to take effect from 1 April 2024. However, the Fund reserves the right to review the stabilisation criteria and limits at any time before then, on the basis of membership and/or employer changes as described above and having regard to the outcome of the current Cost Cap deliberations.

Note (e) **(Maximum time horizon)**

The maximum time horizon starts at the commencement of the revised contribution rate (1 April 2021 for the 2020 valuation). The Fund would normally expect the same period to be used at successive triennial valuations, but would reserve the right to propose alternative time horizons, for example where an employer closed to new entrants over the inter-valuation period.

Following discussion with the Actuary, it is considered that the Fund should target the recovery of any deficit over a period not exceeding 20 years. However, a recovery period of 20 years is not appropriate for all employers. The following table sets out the policy of the Fund;

Type of Employer	**Maximum Length of Time Horizon**
Scheduled Bodies	A period not exceeding 20 years
Community Admission Bodies admitted before 16/5/1975 These employers are: • Dollar Academy Trust • Ballikinrain School	A period not exceeding 20 years (with any cessation debt being shared across the participating Councils)
Community Admission Bodies admitted after 15/5/1975 with a guarantor or providing an essential community wide service across Central Scotland These employers are: • Active Stirling • thinkWhere	A period not exceeding 20 years (with any cessation debt being met by the guarantor or, where one is not available, being shared across the participating Councils)

Community Admission Bodies admitted after 15/5/1975 with neither a guarantor nor providing a community wide service across Central Scotland These employers are: • Snowdon School • Cowane's Hospital • Smith Art Gallery • Water Industry Commissioner • Colleges Scotland	A period equal to the weighted average of the period during which the body's employee members are expected to be active members of the Fund (not . exceeding 10 years). Subject to ratification by the Actuary, the time horizon may be extended depending on the ability and willingness of the employer to make good the deficit over a longer time period.
Closed bodies These employers are: • Scottish Autism	The period during which the body's remaining active members are expected to be active members of the Fund. Subject to ratification by the Actuary, the time horizon may be extended depending on the ability and willingness of the employer to make good the deficit over a longer time period.
Transferee Admission Bodies These employers are: • Cromwell European Management Services • Amey • Forth and Oban Schools • Haven products • Sodexo	The period remaining to the end of the employer's contract (or the weighted average of the period during which the body's employee members are expected to be active members of the Fund if shorter). Where an employer has a small number of active members the Fund will keep the time horizon under regular review – in particular when there are membership changes.

Note (f) (Secondary rate)

The secondary contribution rate for each employer (or, for stabilised employers, the difference between the total stabilised rate and the Primary contribution rate) over the three year period until the next valuation will generally be expressed as a percentage of pay, but may be expressed as monetary amounts (particularly where the employer is closed to new entrants).

Note (g) (Likelihood of achieving funding target)

Each employer has its funding target calculated, 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 higher likelihood will apply due to one or more of the following:

- the Fund believes the employer poses a greater funding risk than other employers;
- the employer does not have tax-raising powers;
- the employer does not have a guarantor or other sufficient security backing its funding position; and/or
- the employer is likely to cease participation in the Fund in the short or medium term.

Note (h) (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 Fund.

In particular, any benefit increases that are agreed following the Cost Cap valuation may result in a review of contribution rates across the Fund.

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

Note (i) (New Admission Bodies)

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, as set out in the LGPS Regulations. 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: For all TABs, the security must be to the satisfaction of the Fund as well as the letting employer, and will be reassessed on an annual basis. See also Note (h) below.

Community Admission Bodies: The Fund will only consider requests from CABs (or other similar bodies) to join the Fund if they are sponsored by a Scheduled Body with tax raising powers, or the Scottish or UK Government, guaranteeing their liabilities and also providing a form of security as above.

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 (j) (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) 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. On admission of a new TAB the pension responsibilities of all parties at the end of the contract (for whatever reason) should be agreed (for example, if at end of the contract the employees revert to the letting employer or to a replacement contractor, who would make any required cessation payment, etc).

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 – fully funded. 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 (i).

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. Clearly as the risk ultimately resides with the employer letting the contract, it is for them to agree the appropriate route with the contractor:

i) Pooling

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) Letting employer retains pre-contract risks

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 at the end of the contract term in respect of assets and liabilities attributable to service accrued during the contract term.

iii) Fixed contribution rate agreed

Under this option the contractor pays a fixed contribution rate throughout its participation in the Fund and does not pay any cessation debt or receive an exit credit. In other words, the pension risks "pass-through" to the letting employer.

The Fund is willing to administer any of the above options as long as the approach is documented in the Admission Agreement as well as the transfer agreement. The Admission Agreement should ensure that some element of risk transfers to the contractor where it relates to its own decisions and it is unfair to burden the letting 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 (k) (Admission Bodies Ceasing)

Notwithstanding the provisions of the Admission Agreement, the Fund 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 Fund 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 Fund 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 following the Local Government Pension Scheme (Scotland) Regulations 2018 which came into effect on 1 May 2018, this will normally result in an exit credit payment to the Admission Body. If a risk-sharing agreement has been put in place (please see note (j) above) no cessation debt or exit credit may be payable, depending on the terms of the agreement.

As discussed in Section 2.7, the LGPS benefit structure from 1 April 2015 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 2015) are confirmed, the Fund's policy is that the actuary will value the employer's liabilities in line with instructions SPPA set out for the 2020 formal valuations.

For Community Admission Bodies whose participation is voluntarily ended either by themselves or the Fund, or where a cessation event has been triggered, the Fund 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:

(a) On the cessation of a pre-1975 Community Admission Body, any deficit will be recovered equally from Clackmannanshire, Falkirk and Stirling Councils;

(b) Where there is a guarantor for future deficits and contributions, or where a robust letter of comfort has been provided from a revenue raising source (i.e. Scottish Government), the details of the guarantee will be considered prior to the cessation valuation being carried out and the cessation may be calculated using the ongoing valuation basis as described in Appendix E; or

(c) Again, depending on the nature of the guarantee, it may be possible to simply pool the former Admission Body's liabilities and assets with the guarantor, without needing to crystallise any debt. This approach may be adopted where the employer cannot pay the contributions due, and this is within the terms of the guarantee;

(d) Where a guarantor does not exist then, in order to protect other employers in the Fund, the cessation liabilities and final deficit/surplus will normally be calculated using a "low risk cessation basis", which is more prudent than the ongoing valuation 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 significant cessation debts being required.

Under (b) and (d), 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 would spread the payment subject to there being 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, and would carry out the cessation valuation on the ongoing valuation basis: secondary contributions would be derived from this cessation debt. This approach would be monitored as part of each 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 low risk exit basis. Furthermore, the Fund reserves the right to revert to a "low risk exit basis" and seek immediate payment of any funding shortfall identified. The Fund may seek legal advice in such cases.

3.4 Pooled contributions

From time to time, with the advice of the Actuary, the Fund may set up pools for employers with similar or complementary characteristics. This will always be in line with its broader funding strategy.

With the advice of the Actuary the Fund allows smaller employers of similar types to pool their contributions as a way of sharing experience and smoothing out the effects of costly but relatively rare events such as ill-health retirements or deaths in service.

Community Admission Bodies that are deemed by the Fund to have closed to new entrants are not usually permitted to participate in a pool. Transferee Admission Bodies are usually ineligible for pooling.

Smaller admitted bodies may be pooled with the letting employer, provided all parties (particularly the letting employer) agree. Employers who left the Fund following the offer of a guarantee from Falkirk, Stirling and Clackmannanshire Councils will have their assets and liabilities pooled with these employers in a 50%/30%/20% proportion.

Employers who are permitted to enter (or remain in) a pool at the 2020 valuation will normally be advised of the contribution rate which applies to them as a member of the pool only, unless otherwise agreed by the Fund.

The intention of the pool is to minimise contribution rate volatility which would otherwise occur when individual 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.

On the other hand it should be noted that 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. This therefore means that if any given employer was funding on a stand-alone basis, as opposed to being in the pool, then its contribution rate could be much higher or lower than the pool contribution rate.

It should also be noted that, if an employer is considering ceasing from the Fund, its required contributions would be based on its own funding position (rather than the pool average), and the cessation terms would also apply: this would mean potentially very different (and in particular possibly much higher) contributions would be required from the employer in that situation.

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

3.5 Additional flexibility in return for added security

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

Such flexibility includes a reduced rate of contribution, an extended time horizon, or permission to join a pool with another body (e.g. the Local Authority).

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.

Please note the legal and actuarial costs of implementing additional flexibility would have to be paid by the employer.

3.6 Non ill health early retirement costs

It is assumed that members' benefits are payable from the earliest age that the employee could retire without incurring a reduction to their benefit (and without requiring their employer's consent to retire). (**NB** the relevant age may be different for different periods of service, following the benefit changes from April 2009 and April 2015). Employers are required to pay additional contributions ('strain') wherever an employee retires before attaining this age. The actuary's funding basis makes no allowance for premature retirement except on grounds of ill-health.

With the agreement of the Fund the payment can be spread over 5 years.

3.7 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 currently met by each employer, although individual employers may elect to take external insurance (see 3.8 below).

Employers will usually have an 'ill health allowance'. The Fund monitors each employer's ill health experience on an ongoing basis. If the cumulative cost of ill health retirement in any financial year exceeds the allowance at the previous valuation, the employer may be charged additional contributions on the same basis as apply for non ill-health cases.

3.8 External Ill health insurance

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

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

The employer must keep the Fund notified of any changes in the insurance policy's coverage or premium terms, or if the policy is terminated. The Fund reserves the right to have the insurance policy assessed by the Actuary or other professional advisors.

3.9 Employers with no remaining active 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 be required to 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 other Fund employers.

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

3.10 Policies on bulk transfers

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

- Where only active members transfer out, the Fund will not pay bulk transfers greater than the value of the members' liabilities had they opted to transfer on an individual basis (i.e. Cash Equivalent Transfer Values);
- Where the entire membership of the employer (i.e. active, deferred and pensioner members) transfers out, the Fund will not pay a bulk transfer greater than the asset share of the transferring employer;
- 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 over the years, 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 Fund after taking investment advice. The precise mix, manager make up and expected returns are set out in the Statement of Investment Principles, which is available to members and employers.

The investment strategy is set for the long-term, but is reviewed from time to time. Investment strategy is monitored on an ongoing basis as part of the Fund's investment governance arrangements. Normally a full review is carried out between actuarial valuations to ensure that it remains appropriate to the Fund's liability profile.

The same investment strategy is currently followed for all employers.

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 policy is consistent with the current investment strategy of the Fund. The actuary's assumptions for future investment returns (described further in Appendix E) are based on the current benchmark investment strategy of the Fund. The future investment return assumptions underlying each of the Fund's funding bases include a margin for prudence, and are therefore also 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 assessments at 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 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 Fund monitors the relative funding position, i.e. changes in the relationship between asset values and the liabilities value, annually. It reports this to the regular joint Board and Pensions Committee meetings, and also to employers and members.

The Fund also monitors the cashflow position of the Fund (e.g. income into and payments from the Fund), ensuring this is considered in both funding and investment strategy,

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 the Scottish Public Pensions Agency (SPPA) acting on behalf of Scottish Ministers, on each of the LGPS Funds in Scotland. This report will cover whether, for each Fund, the rate of employer contributions are set at an appropriate level to ensure both the solvency and the long term cost efficiency of the Fund.

This additional SPPA 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, SPPA 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; and
3. 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.

SPPA may assess and compare these and other 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 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 an FSS is contained in LGPS Regulations which are updated from time to time. In publishing the FSS the Fund 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.

This is the framework within which the Fund's actuary carries out triennial valuations to set employers' contributions and provides recommendations to the Fund 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 Fund consult anyone on the FSS?

Yes. This is required by LGPS Regulations. It is covered in more detail by the most recent CIPFA 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 26 October 2020 for comment;

b) Comments were requested from employers in tandem with discussions relating to each organisations funding position;

c) Questions regarding the FSS could be raised by employers at any time during this engagement period

d) Following the end of the consultation period the FSS was updated where required and then published, in to be updated.

A3 How is the FSS published?

The FSS is made available through the following routes:

- Published on the website, at www.falkirkpensionfund.org;
- A copy included as part of Committee papers and available to all Committee and Board members including employee and pensioner representatives;
- A link to the document in the annual report and accounts of the Fund;
- Copies made available 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 every three years as part of the triennial valuation. 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 within the three year period. 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, any changes other than those of a trivial nature would need the agreement of the Pensions Committee and would be confirmed 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 Statement of Investment Principles and Governance Compliance Statement. 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.falkirkpensionfund.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 Fund should:-

1. operate in accordance with the LGPS (Scotland) Regulations;
2. effectively manage any potential conflicts of interest arising from its dual role as Administering Authority and a Fund employer;
3. collect employer and employee contributions, and investment income and other amounts due to the Fund;
4. ensure that cash is available to meet benefit payments as and when they fall due;
5. pay from the Fund the relevant benefits and entitlements that are due;
6. invest surplus monies (i.e. contributions and other income which are not immediately needed to pay benefits) in accordance with the Fund's Statement of Investment Principles (SIP) and LGPS (Scotland) Regulations;
7. communicate appropriately with employers so that they fully understand their obligations to the Fund;
8. take appropriate measures to safeguard the Fund against the consequences of employer default;
9. manage the valuation process in consultation with the Fund's actuary;
10. provide data and information as required by the Government Actuary's Department to carry out their statutory obligations (see Section 5);
11. prepare and maintain a FSS and a SIP, after consultation;
12. notify the Fund's actuary of material changes which could affect funding (this is covered in a separate agreement with the actuary); and
13. monitor all aspects of the fund's performance and funding and amend the FSS and SIP as necessary and appropriate.

B2 The Individual Employer should:-

1. deduct contributions from employees' pay correctly;
2. pay all contributions, including their own as determined by the actuary, promptly by the due date;
3. have a policy on discretions and exercise these within the regulatory framework;
4. make additional contributions in accordance with agreed arrangements in respect of, for example, augmentation of scheme benefits, early retirement strain; and
5. notify the Fund promptly of all changes to its circumstances, prospects or membership, which could affect future funding.

B3 The Fund Actuary should:-

1. prepare valuations, including the setting of employers' contribution rates. This will involve agreeing assumptions with the Fund, having regard to the FSS and LGPS (Scotland) Regulations, and targeting each employer's solvency appropriately;
2. provide data and information as required by the Government Actuary's Department to carry out their statutory obligations (see Section 5);

3. 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);
4. prepare advice and calculations in connection with bulk transfers and individual benefit-related matters;
5. assist the Fund in considering possible changes to employer contributions between formal valuations, where circumstances suggest this may be necessary;
6. advise on the termination of employers' participation in the Fund; and
7. fully reflect actuarial professional guidance and requirements in the advice given to the Fund.

B4 Other parties:-

1. investment advisers (either internal or external) should ensure the Fund's SIP remains appropriate, and consistent with this FSS;
2. investment managers, custodians and bankers should all play their part in the effective investment (and dis-investment) of Fund assets, in line with the SIP;
3. 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;
4. governance advisers may be appointed to advise the Fund on efficient processes and working methods in managing the Fund;
5. 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 Fund's own procedures; and
6. the SPPA/Scottish Ministers (assisted by the Government Actuary's Department) and the Scottish LGPS Scheme Advisory Board, should work with LGPS Funds to meet Section 13 requirements.

Appendix C – Key risks and controls

C1 Types of risk

The Fund 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

Risk	Summary of Control Mechanisms
Fund assets fail to deliver returns in line with the anticipated returns underpinning the valuation of liabilities and contribution rates 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 three yearly valuations for all employers. Inter-valuation monitoring 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; reviewed at least every three years.
Active investment manager under-performance relative to benchmark.	Quarterly investment monitoring analyses market performance and active managers relative to their index benchmark.
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. The McCloud remedy will extend

Risk	Summary of Control Mechanisms
	the final salary scheme underpin to a further group of members which will increase this risk.
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 debt (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).
Effect of possible asset underperformance as a result of climate change	Climate change scenarios have been considered as part of the modelling exercise to set contributions. The Fund have undertaken a carbon tracking exercise and include climate change risk as part of the quarterly calls with investment managers.

C3 Demographic risks

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. The Fund is able to adopt life expectancy assumptions that are tailored to the membership profile of the Fund through its membership of Club Vita.
Maturing Fund – i.e. proportion of contributing employees declines relative to retired employees.	Continue to monitor at each valuation, capacity to receive monetary amounts in respect of deficits rather than % of pay
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

Risk	Summary of Control Mechanisms
	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 (d) to 3.3). For other employers, review of contributions is permitted in general between valuations (see Note (h) to 3.3.

C4 Regulatory risks

Risk	Summary of Control Mechanisms
Changes to national pension requirements and/or HMRC rules e.g. changes arising from public sector pensions reform.	The Fund considers all consultation papers issued by the Government and comments where appropriate. In particular, known risks are the remedies to the McCloud and Goodwin cases.
Time, cost and/or reputational risks associated with any SPPA/Scottish Ministers intervention triggered by the Section 13 analysis (see Section 5).	Take advice from Fund Actuary on proposed valuation approach relative to anticipated Section 13 analysis.
Changes by Government to particular employer participation in LGPS Funds, leading to impacts on funding and/or investment strategies.	The Fund 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.
Changes to the benefit structure following the Cost Cap valuation carried out by the Government Actuary's valuation	Take advice from the Fund Actuary on considering any related benefit change uncertainty when setting contributions.

C5 Governance risks

Risk	Summary of Control Mechanisms
The Fund 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 Fund 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 Fund 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.
The Fund failing to commission the Fund Actuary to carry out a termination valuation for a departing Admission Body.	The Fund requires employers with outsourced services contracts to inform it of forthcoming changes. Community Admission Bodies' memberships are monitored and, if active membership decreases, steps will be taken.
An employer ceasing to exist with insufficient funding or adequacy of a bond.	The Fund 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 (i) and (k) 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.

Risk	Summary of Control Mechanisms
	Reviewing bond or guarantor arrangements at regular intervals (see Note (h) to 3.3). Reviewing contributions well ahead of cessation if thought appropriate (see Note (c) to 3.3). Regular monitoring of employer risk and covenant
An employer ceasing to exist resulting in an exit credit being payable by the Fund	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.

Section 2 outlined that the setting of an employer's contribution rate was a three step process, as follows:

1. The **funding target** is based on a set of assumptions about the future, eg investment returns, inflation, pensioners' life expectancies. However, 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 of participation;

2. The **time horizon** required is, in broad terms, the period over which any deficit is to be recovered. A shorter period will lead to higher contributions, and vice versa (all other things being equal). 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

3. The required **probability 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, or potentially ceasing from the Fund, then the required probability will be set higher, which in turn will increase the required contributions (and vice versa).

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 contribution 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 funding position and membership. The whole Fund position, including that used in reporting to SPPA (see section 5), is calculated in effect as the sum of all the individual employer rates. SPPA currently only regulates at whole Fund level, without monitoring individual employer positions.

D2 How is the Primary contribution 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 Primary 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), and

3. with a sufficiently high probability, as set by the Fund's strategy for the category of employer (see 3.3 Note (g) 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 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. The measured 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 probability.

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 contribution rate calculated?

The combined Primary and Secondary rates aim to achieve the employer's funding target, within the appropriate time horizon, with the relevant degree of probability.

For the funding target, the Fund actuary agrees the assumptions to be used with the Fund – see Appendix E. These assumptions are used to calculate the present value of all benefit payments expected in the future, relating to that employer's current and former employees, based on pensionable service to the valuation date only (i.e. ignoring further benefits to be built up in the future).

The Fund operates the same target funding level for all employers of 100% of its accrued liabilities valued on the ongoing basis, unless otherwise determined (see Section 3).

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

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

The projections are carried out using an economic modeller developed by the Fund Actuary: 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. The measured contributions are calculated such that the proportion of outcomes with at least 100% solvency (by the end of the time horizon) is equal to the required probability.

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;
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 probability of achieving the funding target.

D5 How is each employer's asset share calculated?

The Administering Authority does not operate separate bank accounts or investment mandates for each employer. Therefore it cannot account for each employer's assets separately. Instead, the Fund Actuary must apportion the assets of the whole Fund between the individual employers. There are broadly two ways to do this:

1) A technique known as "analysis of surplus" in which the Fund actuary estimates the surplus/deficit of an employer at the current valuation date by analysing movements in the surplus/deficit from the previous actuarial valuation date. The estimated surplus/deficit is compared to the employer's liability value to calculate the employer's asset value. The actuary will quantify the impact of investment, membership and other experience to analyse the movement in the surplus/deficit. This technique makes a number of simplifying assumptions due to the unavailability of certain items of information. This leads to a balancing, or miscellaneous, item in the analysis of surplus, which is split between employers in proportion to their asset shares.

2) A 'cashflow approach' in which an employer's assets are tracked over time allowing for cashflows paid in (contributions, transfers in etc.), cashflows paid out (benefit payments, transfers out etc.) and investment returns on the employer's assets.

Until 31 March 2017 the Administering Authority used the 'analysis of surplus' approach to apportion the Fund's assets between individual employers.

Since then, the Fund has adopted a cashflow approach for tracking individual employer assets.

The Fund Actuary tracks employer assets on an annual basis. Starting with each employer's assets from the previous year end, cashflows paid in/out and investment returns achieved on the Fund's assets over the course of the year are added to calculate an asset value at the year end. The approach has some simplifying assumptions in that all cashflows and investment returns are assumed to have occurred uniformly over the course of the year. As the actual timing of cashflows and investment returns are not allowed for, the sum of all employers' asset values will deviate from the whole fund asset total over time (the deviation is expected to be minor). The difference is split between employers in proportion to their asset shares at each triennial valuation.

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

Under the cashflow 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.

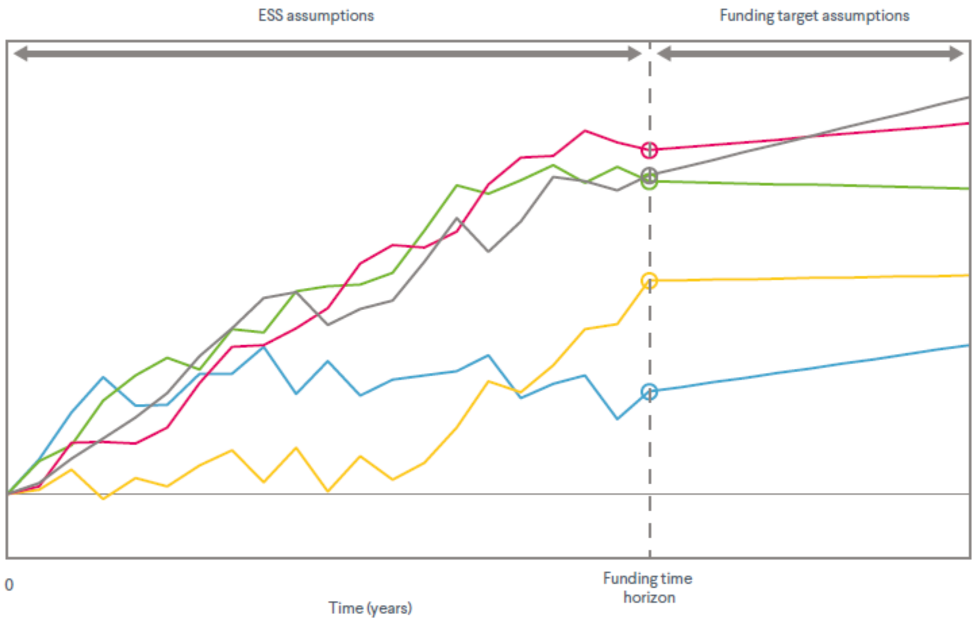
Changes in assumptions will affect the funding target and required contribution rates. However, different assumptions will not of course affect the actual benefits payable by the Fund in future.

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 cashflows 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").

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.



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 2020. 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.

		Annualised total returns									
		Cash	Index Linked Gilts (medium)	Fixed Interest Gilts (medium)	UK Equity	Overseas Equity	Property	A rated Corporate Bonds (medium)	Inflation	17 year real yield	17 year yield
5 years	16th %'ile	-0.6%	-3.0%	-2.9%	-5.3%	-5.2%	-3.7%	-2.1%	1.3%	-2.7%	0.2%
	50th %'ile	0.2%	0.0%	-0.3%	3.7%	3.9%	2.1%	1.3%	2.8%	-1.8%	1.3%
	84th %'ile	1.0%	3.0%	2.5%	13.6%	13.4%	8.7%	4.5%	4.3%	-0.9%	2.5%
10 years	16th %'ile	-0.4%	-2.5%	-2.0%	-2.1%	-2.1%	-1.8%	-1.1%	1.4%	-2.2%	0.6%
	50th %'ile	0.6%	-0.4%	-0.5%	4.3%	4.3%	2.5%	0.8%	2.9%	-0.9%	2.0%
	84th %'ile	1.7%	1.8%	1.0%	10.7%	10.5%	7.2%	2.6%	4.6%	0.3%	3.8%
20 years	16th %'ile	0.2%	-1.5%	-0.6%	0.6%	0.8%	0.2%	0.2%	1.4%	-1.6%	1.2%
	50th %'ile	1.6%	0.2%	0.2%	5.2%	5.3%	3.6%	1.3%	2.9%	0.1%	3.1%
	84th %'ile	3.3%	1.9%	1.0%	9.9%	10.0%	7.4%	2.4%	4.5%	1.9%	5.7%
	Volatility (Disp) (1 yr)	0%	7%	8%	27%	28%	14%	10%	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 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	Low risk 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 1.8% p.a.	An assumption that is consistent with the methodology 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 significance used in both the projection of the assets, benefits and cashflows and in the funding target.

a) Salary growth

The salary increase assumption at the 2020 valuation has been set to be a blended rate combined of:

1. 3% p.a. until 31 March 2025, followed by

2. 0.5% above the consumer prices index (CPI) p.a. thereafter.

This gives a single "blended" assumption of CPI plus 0.6%. This is a change from the previous valuation, which used a salary increase assumption of RPI less 0.5% per annum. The change has led to a slight 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.

As at the previous valuation, we derive our assumption for RPI from market data as the difference between the yield on long-dated fixed interest and index-linked government bonds. This is then reduced to arrive at the CPI assumption, to allow for the "formula effect" of the difference between RPI and CPI. At the previous valuation we assumed CPI would be 1.0% lower than RPI on overage. At the 2020 valuation, we have assumed that CPI will be 0.9% per annum lower than RPI on average, which will serve to increase the funding target (all other things being equal). (Note that the reduction is applied in a geometric, not arithmetic, basis).

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 2019 version of the Continuous Mortality Investigation model published by the Actuarial Profession and a 1.5% per annum minimum underpin to future reductions in mortality rates. This results in slightly lower life expectancies than was assumed at the 2017 valuation.

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 all employers (on the ongoing participation basis identified above), 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.

Full details of all the assumptions used in the funding process will be set out in the most up to date triennial Valuation Report. This can be found at www.falkirkpensionfund.org.

Appendix F – Glossary

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.
Administering Authority	The council with statutory responsibility for maintaining a pension fund.
Admission Bodies	Employers where there is an Admission Agreement setting out the employer's obligations. 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 (and willingness) 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.
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**.
Gilt	A UK Government bond, ie 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.
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.

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.

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 contribution 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.

Scheduled Bodies Types of employer explicitly defined in the LGPS Regulations, whose employees must be offered membership of their local LGPS Fund. These include Councils, colleges, some universities, 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).

Secondary contribution rate The difference between the employer's actual and **Primary contribution 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.

The Fund	The term used in this document to describe those responsible for the governance of the pension fund (i.e. Committee, Board and Senior Officers).
Valuation	An actuarial investigation to calculate the liabilities, and usually individual employer Primary and Secondary contribution rates. This is normally carried out in full every three years (last done as at 31 March 2017), 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.