Report on IAS 26 figures

Fund Accounts 31 March 2020, 2021 and 2022

Prepared for	City and County of Swansea Pension Fund
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QAS Institute and Faculty of Actuaries Quality Assurance Scheme

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Fund	City and County of Swansea Pension Fund
Fund Administering Authority	City and County of Swansea
Accounting Date	31 March 2020
2019 Valuation	Actuarial Valuation of the Fund as at 31 March 2019

1 Introduction

Addressee

This report sets out pension cost information required by the Fund Administering Authority in order to meet their disclosure requirements in relation to their pension obligations as specified by the accounting standard, IAS 26.

We have carried out this work in relation to benefits payable from the Fund.

Related Documents

The advice provided in this report is supported by advice contained in the following documents:

- IAS 26 Terms of Reference – whole of Pension Fund accounting 2020 ('Terms of Reference').
- IAS 26 Assumptions Advice - whole of Pension Fund accounting 2020 ('Assumptions Advice').

In addition, the following documents should be referred to:

- Actuarial Valuation at 31 March 2019 – City and County of Swansea Pension Fund dated 31 March 2020 (the '2019 Valuation'), which contains further detail on the demographic assumptions, and
- 'Actuarial Valuation at 31 March 2019 McCloud/Sargeant judgement' dated 18 September 2019, which sets out details on the method used to estimate the McCloud/Sargeant liability.

Background

CIPFA's Code of Practice indicates that the Fund accounts for the year ending 31 March 2020 should disclose the "actuarial present value of the promised retirement benefits" as set out in IAS 26 and that the actuarial present value should be calculated on assumptions set in accordance with IAS 19 rather than on the funding assumptions.

CIPFA put forward three options for disclosing the actuarial present value of promised retirement benefits. Further detail on these can be found in our Terms of Reference document noted above.

The Fund Administering Authority has chosen option B which was confirmed to us in an e-mail dated 5 May 2020. Option B requires the actuarial valuation of the liabilities on an IAS 19 basis to be prepared at formal triennial valuations only, the most recent being as at 31 March 2019. Under option B this, together with other related information, should be disclosed in the notes to the accounts.

The calculations contained in this document have been carried out on a basis consistent with our understanding of IAS 19.

I confirm that I am an independent qualified actuary.

Document structure

This document is structured as follows:

- Section 1 summarises the scope of the work we have undertaken.
- Section 2 sets out the results of our calculations together with some comments on the calculations.
- Appendix A summarises the data used in our calculations.
- Appendix B sets out a brief explanation of the method we have used in preparing the figures.
- Appendix C sets out compliance and legal considerations.

Methodology

The approach to our calculations under the various options was set out in the Terms of Reference.

Comments on the methodology as it applies to IAS 26 are set out as Appendix B.

2 Information required for IAS 26

Introduction

IAS 26 requires the 'actuarial present value of the promised retirement benefits' to be disclosed, which is the IAS 26 terminology for what IAS 19 refers to as the 'defined benefit obligation'.

The information set out below relates to the actuarial present value of the promised retirement benefits in the Fund which is part of the Local Government Pension Scheme.

The LGPS is a funded defined benefit plan with benefits earned up to 31 March 2014 being linked to final salary. Benefits after 31 March 2014 are based on a Career Average Revalued Earnings scheme. Details of the benefits covered by these figures are set out in 'The Local Government Pension Scheme Regulations 2013' (as amended) and 'The Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014' (as amended).

Actuarial present value of promised retirement benefits (defined benefit obligation)

CIPFA's Code of Practice on local authority accounting for 2019/20 sets out that the actuarial present value of promised retirement benefits based on projected salaries should be disclosed, consistent with the requirements of IAS 19.

The results as at 31 March 2019, together with the results as at 31 March 2016 are shown in the table below. The corresponding fair value of Fund assets is also shown in order to show the level of surplus or deficit within the Fund when the liabilities are valued using IAS 19 assumptions.

We do not believe the Fund Administering Authority needs to show the 2016 figures under IAS 26 if it does not wish to do so. The Code of Practice is not clear if the fair value of assets and the surplus / deficit at 31 March 2019 also needs to be disclosed but you may want to include these figures for clarity.

	Value as at 31 March 2019 £M	Value as at 31 March 2016 £M
Fair value of net assets	2,044.0	1,512.6
Actuarial present value of the defined benefit obligation (see Notes)	3,215.9	2,249.7
Surplus / (deficit) in the Fund as measured for IAS 26 purposes	(1,171.9)	(737.1)

Notes

McCloud / Sargeant judgement

The actuarial present value of the defined benefit obligation at 31 March 2019 includes an estimated liability in relation to the McCloud/Sargeant judgement of £35.2M.

The McCloud/Sargeant judgement (December 2018) found that the transitional arrangements put in place when the Firefighters' and Judges' Pension Schemes were reformed constituted illegal discrimination. The Government has since committed to compensate members of all public service schemes who were illegally discriminated against. In relation to the LGPS in England and Wales all members joined the new 2014

Scheme for membership after 1 April 2014, but members within 10 years of normal retirement were given an underpin (or 'better of both') promise, so their benefits earned after 1 April 2014 would be at least as valuable in terms of amount and when they could be drawn, as if they had remained in the 2008 Scheme.

The remedy for the LGPS is expected to be consulted upon in the summer. The additional liability included within this note assumes the underpin will be extended to cover all members who were actively participating in the Scheme on 1 April 2012 (and not just those within 10 years of retirement).

Equalisation and Indexation of Guaranteed Minimum Pensions

The actuarial present value of the defined benefit obligation includes an estimated liability in relation to the equalisation and indexation of Guaranteed Minimum Pensions (GMPs) beyond the arrangements already formally in place, which apply to members whose State Pension Age (SPA) is between 6 April 2016 and 5 April 2021 inclusive. Those arrangements require the LGPS to pay pension increases on GMPs at the full rate of CPI for those members, whereas GMP legislation only requires limited price increases to be applied. The additional liability included within this note assumes those arrangements for fully indexing GMPs will be extended to members whose SPA is after 5 April 2021. This has increased the defined benefit obligation by in the region of 0.1% to 0.3%.

Cost Management Process

The actuarial present value of the defined benefit obligation does not allow for any potential additional liability which may arise from the cost management valuations.

Legislation requires HM Treasury and the Scheme Advisory Board (SAB) to undertake periodic valuations to monitor the cost of the LGPS to ensure it remains sustainable and affordable.

HM Treasury and the SAB have paused their reviews following the 'McCloud' judgement in the Court of Appeal. The cost cap process will not recommence until the remedy as applies to the LGPS has been decided.

On 24 April 2020 a number of Trades Unions filed court proceedings to challenge the Government’s decision to pause the cost management process. If successful this could lead to higher liabilities and employer costs although it is not yet known how such changes, and those required due to the McCloud case, will affect the cost management valuation due as at 31 March 2020 which it is expected would lead to changes in benefits and/or member contributions in future.

Assumptions

The latest full triennial actuarial valuation of the Fund's liabilities was carried out as at 31 March 2019. The principal assumptions used for the purpose of IAS 26 by the Fund's independent qualified actuaries were:

	31 March 2019 (% p.a.)	31 March 2016 (% p.a.)
Discount rate	2.4	3.4
CPI Inflation (pension increases) *	2.2	1.8
Rate of general increase in salaries **	3.7	3.3

** In excess of Guaranteed Minimum Pension increases in payment for members whose State Pension Age is on or before 5 April 2016 where appropriate*
*** In addition, allowance has been made for the same age related promotional salary scales as used at the actuarial valuation of the Fund as at the appropriate date*

Principal demographic assumptions

The mortality assumptions are based on actual mortality experience of members within the Fund based on analysis carried out as part of the 2019 Actuarial Valuation and allow for expected future mortality improvements. Sample life expectancies at age 65 in normal health resulting from these mortality assumptions are shown below complete with comparative figures from the previous valuation:

	31 March 2019	31 March 2016
Males		
Future lifetime from age 65 (pensioners currently aged 65)	22.1	22.8
Future lifetime from age 65 (actives currently aged 45)	23.1	24.4
Females		
Future lifetime from age 65 (pensioners currently aged 65)	24.1	24.3
Future lifetime from age 65 (actives currently aged 45)	25.6	26.1

Different mortality assumptions have been used for other categories of member as set out in the actuary's report on the 2019 valuation. Assumptions for the rates of the rates of withdrawal and ill health retirements (for active members), the allowance made for cash commutation on retirement, and the proportion of members whose death gives rise to a dependant's pension are the same as those adopted in the 2019 valuation of the Fund, which are detailed in the actuary's report on the 2019 valuation.

Key risks associated with reporting under IAS 26 and sensitivity

Volatility of results

Results under IAS 26 can change dramatically depending on market conditions. The defined benefit obligation is linked to yields on AA-rated corporate bonds, while a significant proportion of the assets of the Fund are invested in equities and other growth assets. Changing markets in conjunction with discount rate volatility will lead to volatility in the funded status of the pension fund. For example:

- A decrease in corporate bond yields will increase the value placed on the liabilities for accounting purposes, although this will be marginally offset by the increase in the assets as a result (to the extent the Fund invests in corporate bonds).
- The majority of the pension liabilities are linked to either pay or price inflation. Higher inflation expectations will lead to a higher liability value. The assets are not perfectly correlated with inflation meaning that an increase in inflation will increase the deficit.

- The majority of the Fund's obligations are to provide benefits for the life of the member following retirement, so increases in life expectancy will result in an increase in the liabilities.

If at any time during the year you want us to provide you with an update of the IAS 26 position, please let us know.

Choice of accounting assumptions

The calculation of the actuarial present value of the promised retirement benefits involves projecting future cash-flows from the Fund many years into the future. This means that the assumptions used can have a material impact on the surplus / deficit. As such, the Fund Administering Authority should ensure that it understands the reasoning behind the assumptions adopted and is comfortable that they are appropriate.

Furthermore, the Fund Administering Authority should bear in mind that, as required by the accounting standard, the assumptions (with the exception of the discount rate) have been set so that they represent a best estimate of future experience from the Fund. In practice future experience within the Fund may not be in line with the assumptions adopted. This means that the liabilities shown in this report only represent one view of the future and the true position could be different from those shown. For example, members could live longer than expected or inflation could be higher or lower than allowed for in the calculations.

Sensitivity of results to key assumptions

In order to understand the magnitude of the possible volatility in the balance sheet position and to understand which assumptions are most important in determining the size of the liabilities, it is helpful to understand how sensitive the results are to the key assumptions.

IAS 19 requires entities to disclose information about the sensitivity of the defined benefit obligation to changes in key assumptions although it is not clear that IAS 26 or the CIPFA Code of Practice requires this information. Nevertheless, we have set out below how the results would alter by changing the discount rate, the pay increase assumption and pension increase assumption by plus or minus 0.1% and if life expectancy was to reduce or increase by 1 year. In each case, only the assumption mentioned is altered; all other assumptions remain the same.

Sensitivity Analysis

Discount rate assumption		
Adjustment to discount rate assumption	**+0.1% £M**	**-0.1% £M**
£ change to present value of the defined benefit obligation	(66.592)	68.000
% change in present value of defined benefit obligation	(2.1%)	2.1%

Rate of general increase in salaries		
Adjustment to salary increase rate assumption	**+0.1% £M**	**-0.1% £M**
£ change to present value of the defined benefit obligation	10.633	(10.511)
% change in present value of defined benefit obligation	0.3%	(0.3%)

Rate of increase to pensions in payment, deferred pensions increase assumption and rate of revaluation of pension accounts		
Adjustment to pension increase rate assumption	**+0.1% £M**	**-0.1% £M**
£ change to present value of the defined benefit obligation	57.367	(56.081)
% change in present value of defined benefit obligation	1.8%	(1.7%)

Post retirement mortality assumption		
Adjustment to post retirement mortality assumption	**- 1 year £M**	**+ 1 year £M**
£ change to present value of the defined benefit obligation	(99.478)	100.454
% change in present value of defined benefit obligation	(3.1%)	3.1%

Appendix A – Membership data

The results in this report are based on membership data which is summarised below. The 2016 figures are provided for comparison:

Active members		Number	Average age	Total pensionable salaries (2014 scheme definition) (£000 p.a.)	Total pre 2014 pension (£000 p.a.)	Total pre 2014 accrued lump sum (£000)	Total post 2014 pension (£000 p.a.)
2016	Male	5,187	45.3	112,833	20,196	36,220	4,174
	Female	12,048	44.3	153,870	22,168	34,116	5,763
	Total	**17,235**	**44.6**	**266,703**	**42,364**	**70,336**	**9,937**
2019	Male	5,712	45.2	119,634	16,878	29,005	10,598
	Female	14,120	44.5	174,394	19,353	28,948	14,613
	Total	**19,832**	**44.7**	**294,028**	**36,231**	**57,953**	**25,211**

Notes: *The average ages are unweighted.*

Pensionable pay is over the year to the valuation date and includes annualised pay for new entrants during the year.

Actual part-time pay is included for part-timers.

Post 2014 pension figures include the April 2019 (2016: April 2016) revaluation.

Deferred members		Number	Average age	Total pension (£000 p.a.)	Total pre 2014 accrued lump sum (£000)
2016	Male	3,381	43.6	5,880	13,435
	Female	7,913	43.9	8,012	16,144
	Undecided	1,853	-	-	-
	Total	**13,147**	**43.8**	**13,892**	**29,579**
2019	Male	3,474	44.6	6,705	12,737
	Female	8,404	45.0	10,045	15,821
	Undecided	2,532	43.7	557	582
	Total	**14,410**	**44.8**	**17,307**	**29,140**

Notes: The average ages are unweighted.

The deferred pension amounts shown above are at the valuation date and include the April 2019 (2016: April 2016) revaluation.

Pensioner members		Number	Average age	Total pension (£000 p.a.)	Average pension (£ p.a.)
2016	Male	4,099	70.0	31,662	7,724
	Female	6,079	69.6	20,843	3,428
	Dependants	1,594	71.7	4,664	2,926
	Total	**11,772**	**70.1**	**57,169**	**4,856**
2019	Male	4,439	70.5	35,795	8,064
	Female	7,082	70.1	25,768	3,639
	Dependants	1,702	72.2	5,076	2,982
	Total	**13,223**	**70.5**	**66,653**	**5,041**

Notes: The pension amounts shown above include the increase awarded in April of the appropriate year.
Average ages are unweighted.
Figures include members in receipt of a child's pension.

Appendix B - Explanation of actuarial methods used

Benefits valued

Our calculations relate to benefits payable from the Fund (as set out in LGPS Regulations at the relevant times – further details can be found in the 2019 valuation report). These benefits include retirement pensions and benefits on members' death and leaving service. In addition, we have made allowance for the McCloud / Sargeant judgement and GMP indexation / equalisation as set out in the Terms of Reference.

Unfunded defined benefit obligations e.g. discretionary pensions benefits being paid under the Local Government (Early Termination of Employment) (Discretionary Compensation) Regulations (generally referred to as Compensatory Added Years), have not been valued as they do not form part of the Fund. However, they may be required in the IAS 19 figures prepared for individual employers within the Fund.

Data

The valuation of accrued pension benefits for IAS 26 purposes requires detailed information in respect of each member such as date of birth, gender, date of joining the fund, their accrued pension and so forth.

This information was supplied by the Fund Administering Authority for the 2019 formal actuarial valuation of the Fund in the form of a standardised data extract from the Fund Administering Authority's administration systems.

The formal valuation process (which is a precursor to the valuation for IAS 26 purposes) involves a series of structured validation tests on the data items for integrity and reasonableness. These tests, together with any actions taken in respect of specific data issues, are documented as part of the normal valuation process.

Where tests reveal issues with the data, the Fund Administering Authority is contacted with a view to resolving all data queries. Only when the data queries have been resolved to the satisfaction of the Fund Actuary, will the valuation proceed.

We can confirm that no data issues were identified at the 2019 valuation that we believe would have a material effect on the calculations presented in this report. Overall, it is our opinion that the data presented at the valuation is sufficiently accurate, relevant and complete for the Fund Administering Authority to rely on the resulting IAS 19 (IAS 26) figures.

Assumptions

IAS 19 sets out the following general requirements for the setting of assumptions:

- Actuarial assumptions shall be unbiased and mutually compatible; and
- Financial assumptions shall be based on market expectations, at the balance sheet date, for the period over which the obligations are to be settled.

Furthermore IAS 19 requires that the assumed discount rate is determined by reference to market yields at the balance sheet date on high quality corporate bonds and in countries where there is no deep market in such bonds, the market yield (at the balance sheet date) on government bonds shall be used.

CIPFA have informed us that under IAS 26 the assumptions are ultimately the responsibility of the Fund Administering Authority. Any assumptions that are affected by economic conditions (financial assumptions) should reflect market expectations at the balance sheet date.

The key financial assumptions are set out on the first page of Section 2 and the derivation of the assumptions is set out in our assumptions letter referred to in the Related Documents section.

Method of calculation

The figures at 31 March 2019 have been based on a full calculation of the liabilities using the data summarised in this report and the assumptions set out in the Assumptions Advice. Further information on the method was set out in the Terms of Reference.

Assets

IAS 19 requires that assets be valued at Fair Value which is defined as the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction. For the purposes of this exercise we have taken the asset values directly from the Fund's audited annual accounts as at 31 March 2019.

The assets do not include Additional Voluntary Contributions.

Treatment of Risk Benefits

To value the risk benefits we have valued service related benefits based on service completed to the date of calculation only.

Expenses

Fund administration expenses are not reserved for in the Net Present Value of Actuarial Liabilities, consistent with the treatment adopted for individual employers who require IAS 19 disclosures. If the Fund wishes the administration expenses to be treated in a different way they should discuss this further with their auditor and ourselves.

IFRIC 14

IFRIC 14 is an interpretation of paragraph 58 of the IAS 19 accounting standard setting out limits to the amount of surplus that can be recognised by employing organisations in their accounts. We do not believe it has any relevance to IAS 26.

Appendix C – Compliance and disclaimer

Compliance with actuarial standards

The documents set out in section 1 under the heading 'Related documents', together with this report and the work relating to it, is subject to, and complies with the Financial Reporting Council Limited's Technical Actuarial Standard 100: Principles for Technical Actuarial Work ('TAS 100').

The compliance is on the basis that City and County of Swansea Council is the addressee and the only user, and that the report is only to be used for the purposes of disclosure of information under IAS 26. If you intend to make any other decisions after reviewing this report, please let us know and we will consider what further information we need to provide to help you make those decisions.

The report has been prepared under the terms of the Agreement between City and County of Swansea Council and Aon Hewitt Limited on the understanding that it is solely for the benefit of the addressees

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Disclaimer

The calculations contained in this report have been made on a basis consistent with our understanding of IAS 19 and IAS 26. Figures required for other purposes should be calculated in accordance with the specific requirements of those purposes. It must not be assumed that figures produced for the purposes of IAS 26, which we present in this report, have any relevance beyond the scope of the Financial Reporting Standards requirements.

This report is prepared on the instructions of the Fund Administering Authority as appropriate ("you" or "your") in relation to the preparation of IAS 26 figures for the Fund Administering Authority's financial reporting as at the Accounting Date. It has been prepared at this date, for the purpose and on the basis set out in this report and for the benefit and use of the Fund Administering Authority.

This report should not be used or relied upon by any other person for any other purpose including, without limitation, other professional advisers, including your auditors and accountants ("third parties" or "third party"), to the Fund Administering Authority. All third parties are hereby notified that this report shall not be used as a substitute for any enquiries, procedures or advice which ought to be undertaken or sought by them. We do not accept any responsibility for any consequences arising from any third party seeking to rely on this report.

We neither warrant nor represent (either expressly or by implication) to any third party who receives this report that the information contained within is fair, accurate or complete, whether at the date of its preparation or at any other time.

Unless we provide express prior written consent, no part of this report should be reproduced, distributed or communicated to any other person other than to meet any statutory requirements and, in providing this report, we do not accept or assume any responsibility for any other purpose or to anyone other than the Fund Administering Authority as appropriate.

We recognise that your auditors may request you directly to see a copy of our report, as part of their audit process and under statutory requirements. We agree that you may release our report to those auditors for such purpose however in making such disclosure, you shall ensure that this disclaimer remains attached to this report, and you further agree that you shall ensure that your auditors have read this disclaimer. For the avoidance of doubt, if we are approached directly by any third party for copies of this report or requested to answer queries about the report, we will require such third party to accept a third party release non reliance letter agreeing that we did not prepare the report for the third party and we do not accept any legal obligations to them. Please rest assured that this approach does not affect our contractual obligations to you as our client, with whom we continue to hold a duty of care in accordance with our terms of engagement.

This report was based on data available to us at the effective date of our calculations and takes no account of developments after that date except where explicitly stated otherwise.

With respect to data on which we have relied in producing this report, whilst we have taken certain limited steps to satisfy ourselves that the data provided to us is of a quality sufficient for the purposes of our investigation, including carrying out certain basic tests for the purpose of detecting manifest inconsistencies, it is not possible for us to confirm the accuracy or completeness of the detailed information provided. Whilst the Fund Administering Authority may have relied on others for the maintenance of accurate data, it is their responsibility to ensure the adequacy of these arrangements and ultimately the Fund Administering Authority that bears the primary responsibility for the accuracy of such information provided. The information used is summarised in various sections of this report and Appendix A.