London Borough of Hammersmith and Fulham Pension Fund

2019 actuarial valuation – Council results

Purpose and scope

We have been requested by the London Borough of Hammersmith and Fulham (the Council), the administering authority of the London Borough of Hammersmith and Fulham Pension Fund (the Fund), to prepare an executive summary of the whole fund valuation results and a summary of the 2019 actuarial valuation results attributable to the Council.

Whole Fund Results

Past service funding position

The following table summarises the funding position attributable to the Fund at 31 March 2019 and compares this with the position at 31 March 2016, the date of the last formal funding valuation.

Past service funding position	31 March 2019	31 March 2016
Assets	£1,044m	£851m
Liabilities	£1,079m	£966m
Surplus / (Deficit)	(£35m)	(£115m)
Funding level	97%	88%

Over the three years to 31 March 2019, investment returns have been very strong, averaging 8.4% p.a. This is higher than assumed at the last valuation (5.4% p.a.) and is the main reason for the increase in funding level, together with paying in additional contributions towards the deficit.

The liabilities have also increased as a result of members accruing more benefit over the 3 years, an assumed lower discount rate and higher future inflation. Future life expectancy improvements have reduced which has dampened the increase on the liabilities.

Proposed contribution rate

Revised contribution rates for all employers in the Fund will take effect from 1 April 2020 and will apply for the three years to 31 March 2023. As required by the LGPS Regulations, the contribution rate for each employer will be presented in two parts:

- Primary contribution rate. This is expressed as a percentage of pensionable pay and reflects the contributions required in order to fund the employer's share of the cost of benefits building up now and in the future (net of employee contributions).
- Secondary contribution rate. This is any percentage or amount by which the primary rate of contribution should be increased or decreased, most commonly in order to pay off any past service deficit which is attributable to the employer or to return an element of surplus to the employer.

The following table summarises the primary rate at whole Fund at 31 March 2019 and compares this with the primary rate at 31 March 2019.

Primary rate	Proposed basis 31 March 2019 % of payroll p.a.	Previous valuation 31 March 2016 % of payroll p.a.
Average total future service rate	24.4%	22.5%
Less average member rate	-7.0%	-7.0%
Fund primary rate	**17.4%**	**15.5%**

The primary rate has increased as a result of the increase in CPI inflation and the decrease in discount rate from 5.4% to 5.0% p.a. This increase has been offset to some extent by the lower assumed future improvements in life expectancy relative to the assumption made at 31 March 2016.

Council results

Past service funding position

The following table summarises the funding position attributable to the Council at 31 March 2019 and compares this with the position at 31 March 2016.

Past service funding position	31 March 2019	31 March 2016
Assets	£925m	£730m
Liabilities	£974m	£865m
Surplus / (Deficit)	(£49)	(£135m)
Funding level	95%	84%

The following table sets out the proposed revised contribution rate for the Council and compares it with the current level of contributions:

Contribution rate	From 1 April 2020	From 1 April 2019
Primary rate (% of pay/amount)	17.1% / £13.9m	15.3% / £11.9m
Secondary rate (% of pay/amount)	4.8% / £3.8m	11.3% / £8.6m
Total rate (% of pay/amount)	**21.9% / £17.7m**	**26.3% / £20.5m**

As can be seen, the primary contribution rate has increased since the last valuation. This is mainly due to changes in assumptions underlying our valuation, in particular because of a lower level of investment returns assumed going forward (i.e. a lower discount rate). Given the strong investment performance experienced by equity markets over the last few years, we are effectively assuming that this may be balanced out by lower investment returns in future. Furthermore, the outlook for future inflation has increased which means that future salary and pension growth are assumed to be higher than at the 2016 valuation. More details on the assumptions adopted can be found in the next section.

The secondary rate reduction has however decreased significantly, from 11.3% to 4.8% reflecting the increase in the funding level and decrease in deficit over the period. This means the total required contribution rate can reduce. In calculating the secondary rate, we have adopted a deficit recovery period of 17 years.

Risks

It is worth noting there are a number of potential additional risks and uncertainties to be aware of, including:

- The possibility of a market correction. There is a risk that the exceptional level of investment returns witnessed over recent years may lead to a “correction” in the markets, causing a deterioration of asset values in future.
- Additional liabilities arising from the recent McCloud and Sargeant cases. There has been a recent Court of Appeal judgement in relation to the McCloud & Sargeant cases which relate to age discrimination within the Judicial & Fire Pension schemes respectively. On 27 June 2019 the Supreme Court denied the Government’s request for an appeal, and on 15 July 2019 the Government released a statement to confirm that it expects to have to amend all public service schemes, including the LGPS. The impact is likely to be an increase in liabilities.
- Additional liabilities arising from the HM Treasury cost cap mechanism. The purpose of the cost cap mechanism is to ensure the cost of the LGPS remains sustainable, however this has recently been triggered. The review found that there has been a reduction in certain costs associated with providing LGPS benefits largely due to a slow down in improvements in longevity and so there is an expectation that benefits will be improved. Any improvements will be subject to the remedy that is decided in light of the recent McCloud & Sargeant judgement.
- Other political and economic uncertainties. There is a great deal of uncertainty in the UK economy at the moment as the UK continues to respond to the results of the European referendum in 2016, leading to a high level of volatility in the equity and currency markets. We consider it more prudent to retain some surplus within the Fund until more stability returns to the economy.

Assumptions

The key financial and demographic assumptions used in our valuation are summarised as follows:

Key assumptions	31 March 2019	31 March 2016
Discount rate	5.0% p.a.	5.4% p.a.
CPI inflation	2.6% p.a.	2.4% p.a.
Salary increases		
Short term	n/a	CPI to 31 March 2020
Long term	3.6% p.a.	3.9% p.a.
Life expectancies (years)		
Male currently aged 65	21.7	24.6
Female currently aged 65	24.3	26.2
Male currently aged 45	23.1	26.9
Female currently aged 45	25.8	28.5

Further details of the assumptions and data used can be found in our report *LBHF March 2019 Initial Results Advice* dated 1 October 2019.

Next steps

We trust the above information is useful and would be happy to answer any queries at our meeting on 15 November. Following agreement of the above contributions, these will be certified in our formal report on the valuation which is due to be completed by 31 March 2020.

Barry McKay

Barry McKay FFA
Barnett Waddingham LLP
12 November 2019