**INTERIM INDEPENDENT AUDIT COMMITTEE**
**28 MARCH 2013**

# ASSUMPTIONS USED IN THE IAS19 PENSION DISCLOSURE 2013/14 ACCOUNTS

## SUMMARY AND PURPOSE OF REPORT

For the Committee to be able to review and comment upon the suitability of the assumptions used by Hymans Robertson actuary when valuing the pension assets and liabilities.

## RECOMMENDATIONS

1. **The Committee note the assumptions being used by Hymans Robertson for the Local Government Pension Scheme;**

2. **The Committee note the general approach being used by Hymans Robertson for the Police Pension Scheme.**

## A. SUPPORTING INFORMATION

1. Introduction

   1.1. IAS19 - Employee Benefits is one of the financial reporting standards that the PCC and Chief Constable must comply with when producing their Annual Accounts. IAS19's basic requirement is that an organisation should account for retirement benefits when it is committed to give them, irrespective of when they are paid out.

   1.2. To calculate the cost of earned benefits for inclusion in the accounts, the scheme Actuary (Hymans Robertson) use certain assumptions to reflect expected future events which may affect those costs. The assumptions used are designed to lead to the best estimate of the future cash flows that will arise under the scheme liabilities. Any assumptions that are affected by economic conditions should reflect market expectations at the balance sheet date.

   1.3. Lincolnshire Police Group's net Pension Liability (the difference between the assets held and projected liabilities) as at 31 March 2013 was calculated at £1,002m. This is a material component of the PCC's balance sheet and therefore its net worth. As such it is important that the PCC group is supportive of the assumptions being made by the actuary in their calculations. This year's net position will be affected by the assumptions used, but does not immediately change ongoing revenue costs.

2. Assumptions

2.1. The calculated costs and the underlying assumptions, based upon the advice of the actuary and the administering authority (Lincolnshire County Council for the LGPS) will be used in preparing the PCC group's 2013/14 Accounts.

2.2. The triennial formal actuarial valuation took place as at 31 March 2013. The Fund's actuary advises that the deficit could be removed over a period of 20 years by increasing the current employer contribution rate of 19.9% to a contribution rate of 25.8%. The minimum required contribution as required by the actuary from April 2014 is the current employer contribution rate of 19.9% plus the following supplementary contributions:

| | | |
|---|---|---|
| 2014/15 | £0.196m | equivalent rate 20.9% |
| 2015/16 | £0.407m | 21.9% |
| 2016/17 | £0.634m | 22.9% |

2.3. The accounting requirements of IAS19 do not require that every individual estimate is a "best estimate". Directors of the organisation should be satisfied that the combined effect of the assumptions as a whole is reasonable.

2.4. Proposed financial assumptions for the Local Government Pension Scheme 2013/14

**IAS19 – LGPS Pensions Assumptions for 31 March 2014**

The value of the Pension Fund's assets and liabilities are heavily dependent on the underpinning assumptions. The employer is ultimately responsible for the assumptions used, and this year's proposed assumptions are listed below. The approach for each of them is detailed in the Actuary's briefing note at **Appendix A**. Where the assumptions rely on market conditions as at 31 March an estimate is shown here based on 31 December 2013. The final figures used will be quoted in the body of the schedule of IAS 19 results:-

- **Discount Rate** – this allows for the effect of inflation on the liabilities in the scheme. There are a range of rates which are based on market conditions as at 31 December. Medium term assets with a duration of 17 to 23 years had a discount rate of 4.4% as at December.

- **Expected Return on Assets** – this is taken from the actuary's proprietary asset model which tracks the market conditions on a monthly basis. At 31 December 2013 the expected return on UK equities was 7.1% p.a..

- **Salary Growth** – long term pay growth is assumed to be linked to the assumed rate of the Retail Price Index (RPI), with an additional allowance for promotional salary increases. December's market conditions placed the RPI at 3.6% for investments less than 23 years duration, 3.7% for any longer.
- **Pension Increases Assumption** – In the LGPS pension increases are linked to the rate of CPI (Consumer Price Index) as opposed to RPI. The

Actuary has assessed the gap between RPI and CPI going forward to be a reduction of 0.8%, giving an assumption of 2.8% p.a. as at March 2014.

- **Demographic Assumptions** – these are the post retirement longevity and mortality assumptions used by the Actuary, and have not changed from previous years.

- **Pensioner Mortality** – this is based on a bespoke set of VitaCurves that are specifically tailored to fit the membership profile of the Fund and are based on data provided to the Actuary at the last formal valuation. As such, they normally change every year. .

- **Commutation –** this allows for the effect of future retirees choosing to take a larger initial lump sum and reduced annual pension. The 2013/14 assumptions are expected to remain with 25% of members who joined the scheme prior to 1 April 2008 and 62.5% of members who joined since that date.

  Other demographic assumptions are used, e.g. rates of withdrawal from the scheme, number of ill-health early retirements, proportion of deaths leaving a dependant, etc.. These assumptions are based on past experience, and are not expected to change from 2012/13.

2.5. Proposed financial assumptions for the Police Government Pension Scheme 2013/14

**IAS19 – Police Pensions Assumptions for 31 March 2014 unavailable, so 2012/13 assumptions presented for information.**

There are no assets in the police schemes. The value of the Pension Fund's liabilities are heavily dependent on the underpinning assumptions. There are no assumptions available for the police scheme until early April. The key factors will be the same as last year and are presented below for information

- **Discount Rate** – this allows for the effect of inflation on the liabilities in the scheme, and has been assumed to be 4.5% as at 31 March 2013, being 3.2% gilt yield plus 1.3% credit spread. This is higher than the iBoxx yield of 4.1% but is believed to be appropriate for IAS19 purposes.

- **Retail Prices Inflation (RPI)** – this is the assumption used as the basis for future salary growth. This is typically derived from the yields available on fixed interest and index linked government bonds – the rate being 3.6% p.a. as at March 2013.

- **Pension Increases Assumption** – Following the announcement in the June 2010 Budget, pension cost increases now follow the Consumer Prices Index (CPI). The Actuary has assessed the gap between RPI and CPI going forward to be a reduction of 0.8%, giving an assumption of 2.8% p.a. as at March 2013.

- **Demographic Assumptions** – these are the post retirement longevity and mortality assumptions used by the Actuary, and have not changed from previous years.

- **Pensioner Mortality** – this impacts on the length of time pensions are expected to be payable, and are unchanged from last year.

- **Retirement age –** in line with last year, it is assumed that officers retire when they reach 30 years of service.

- **Salary scales –** in line with last year, the promotional salary scales are based on published salary scale tables.

- **Salary growth –** in line with last year, the assumption for the rate of increase in pensionable salaries is 1% above CPI, so 3.8%.

- **Retirement age –** in line with last year, it is assumed that officers retire when they reach 30 years of service.

  Other demographic assumptions are used, e.g. rates of withdrawal from the scheme, number of ill-health early retirements, etc. These assumptions are based on past experience, and have not changed from those used in 2011/12.

2.6. There are no direct financial implications as a result of this report, as it sets out the input factors that the actuary uses to calculate the pension position for the PCC and the Chief Constable under IAS 19, showing the estimated net value of the group's portion of the pension fund (assets less liabilities). Changes in assumptions will affect the net position, but this has a nil overall change in the resources available to the PCC on the balance sheet, and any changes to the income and expenditure statement are reversed through statutory accounting entries.

2.7. If an employer wishes to use different financial assumptions the Actuary would impose additional fees.

## B. FINANCIAL CONSIDERATIONS

None.

## C. LEGAL AND HUMAN RIGHTS CONSIDERATIONS

None.

## D. PERSONNEL, EQUAL OPPORTUNITIES AND DIVERSITY ISSUES (including any impact or issues relating to Children and Young People.)

None.

## E. REVIEW ARRANGEMENTS

The actual assumptions used will be available to the Committee at their June meeting.

## F. RISK MANAGEMENT

None.

## G. PUBLIC ACCESS TO INFORMATION

Information in this report along with any supporting material is subject to the Freedom of Information Act 2000 and other legislation.