**METHODIST MINISTERS’ PENSION SCHEME *MC/15/32***

**Draft**

**Statement of Funding Principles**

1. **Status**

This statement was agreed by the Trustee on 5 March 2015 for the purposes of the actuarial valuation as at 1 September 2014 after obtaining the advice of Stephen Ainsworth, the actuary to the Scheme and after consulting with the Finance Sub Group of the Strategy and Resources Committee (SRC) of the Methodist Church. This Statement of Funding Principles replaces the previous Statement dated 1 March 2012 to reflect changes agreed between the Trustee and the SRC.

1. **The statutory funding objective**

This statement sets out the Trustee’s policy for ensuring that the statutory funding objective is met. The statutory funding objective is defined in section 222 of the Pensions Act 2004, which states that every scheme must have sufficient and appropriate assets to cover its technical provisions.

1. **Funding objectives in addition to the statutory funding objective**

None

1. **Calculation of the technical provisions**

4.1 Technical provisions

The technical provisions are the amount that will be needed to pay the Scheme benefits, as set out in the Scheme’s Rules, that relate to service up to the valuation date, if the assumptions made are borne out in practice. The assumptions used to calculate the technical provisions are intended to provide a prudent estimate of the future experience of the Scheme, with a modest allowance for the future potential investment returns above the gilt yield from continued investment in more risky assets. There is an underlying assumption that the Scheme will continue as a going concern with benefits being met from the Scheme as they fall due.

4.2 Method

The actuarial method to be used in the calculation of the technical provisions is the Projected Unit Method.

4.3 Investment strategy

The choice of the discount rates needs to have regard to the investment strategy of the Scheme. The current investment strategy for the Scheme is set out in the Scheme’s Statement of Investment Principles and is reproduced in Appendix 1.

4.4 Assumptions

The discount rate assumptions are determined in the light of the current strategic asset target weighting for each asset class.

Details of the actual economic assumptions to be used to calculate the technical provisions at the valuation date are set out in Appendix 2. Details of the demographic assumptions at the valuation date are set out in Appendix 3.

The following principles are to be applied to determine the economic assumptions:

* **Discount rate:**  The discount rate used to value the liabilities both in the period to retirement and after retirement is determined with reference to the yield on gilts at the valuation date with adjustment to allow for the expected outperformance over gilts allowing for the Scheme’s current investment strategy. The outperformance premiums will be determined as a prudent allowance for the outperformance of the assets relative to the return available on gilts. The premiums will be determined having regard to the Scheme’s investment strategy, the strength of the covenant of the Methodist Church and market conditions at the time of the valuation. The premiums at 1 September 2014 are 2% pa pre retirement and 1% pa post retirement. The premiums will be reviewed at each valuation.
* **Inflation:** The Retail Prices Index (RPI) inflation assumption is taken to be the investment market’s expectations for inflation as derived from the difference between the yield on fixed interest gilts and (RPI) index linked gilts at the valuation date. The Consumer Prices Index (CPI) Inflation assumption is derived from the RPI assumption by making an appropriate adjustment to reflect the differences between RPI and CPI. The difference between the long term assumption for RPI and CPI inflation may vary over time to reflect changing views of long term structural differences between the calculation of RPI and CPI inflation at the date subsequent calculations are carried out. The CPI assumption at 1 September 2014 is derived by deducting 0.7% pa from the RPI assumption.
* **Pension increases:**Pensions in payment are assumed to increase annually by the rate of RPI inflation capped at 5% pa for benefits accrued prior to 31 August 2006 and capped at 2.5% pa for benefits accrued on or after 1 September 2006. Deferred pensions are assumed to increase at the rate of CPI inflation capped at 5% pa over the period of deferment for service prior to 6 April 2009 and with a 2.5% pa cap for service from 6 April 2009. The increases are derived from the price inflation assumptions, allowing for the maximum and minimum annual increases and for inflation to vary from year to year.
* **Stipend increases:** Stipends are assumed to increase at the rate of CPI inflation plus a stipend increase adjustment. This adjustment is 0.75% pa at 1 September 2014 and will be reviewed at each valuation.

The other assumptions will be as follows:

* **Mortality:**Standard published tables of mortality have been adopted that have been found appropriate for the Scheme as a whole. These tables allow for expected future improvements in longevity. Sample rates and the details of the tables are included in Appendix 3 to this statement. The mortality assumptions will be reviewed at each valuation.
* **New entrants:** The valuation method assumes that the membership of the Scheme remains stable. It assumes that people who leave the Scheme are replaced by new joiners, such that the age and sex profile of the membership remains broadly unchanged.
* **Leaving service:** No allowance has been made for withdrawals from service prior to Normal Pension Dates.
* **Retirement:**  Allowance has been made for retirements before Normal Pension Dates and for members retiring in ill health by means of age related scales. Sample rates are included in Appendix 3. This assumption will be reviewed at each valuation.
* **Age difference of dependants:** Allowance will be made for an age differential between the member and their spouse.
* **Percentage with spouse benefits at death:**An allowance will be made for members with spouse benefits at death.
* **Commutation**: Allowance will be made for members to commute part of their pensions at retirement for a lump sum. This allowance is 15% of main Scheme pensions at 1 September 2014. This allowance will be reviewed at each valuation.
* **Management expenses**: Allowance will be made for the expected expenses of the Scheme. This allowance is summarised in Appendix 3 and will be reviewed at each valuation.

1. **Covenant of the Methodist Church**

The method and assumptions used to calculate the technical provisions at the 1 September 2014 valuation assume a continuation of the covenant of the Methodist Church as strong. If this changes significantly the Trustee would wish to review the method and assumptions.

1. **Church contributions**

The contributions payable by the Circuits are assessed by calculating the cost of future benefit accrual using the same assumptions as for the technical provisions, plus an estimate of the expenses (excluding investment-related expenses) including the Pension Protection Fund levy, reduced by the contributions made by members and adjusted by the amounts needed to eliminate any shortfall or surplus relative to the technical provisions.

1. **Policy on discretionary increases and funding strategy**

Pensions may be increased from time to time once in payment by an amount over and above the guaranteed rate of increases set out in the Rules, having regard to the financial position of the Scheme, at the discretion of the Trustee after consultation with the actuary and with consent of Conference.

Advance provision is not to be made for any discretionary increases for the purpose of calculating the technical provisions. If discretionary increases to benefits are to be made, the Trustee’s current policy would be to request immediate additional contributions to meet the cost of such increases.

1. **Period within which and manner in which a failure to meet the statutory funding objective is to be rectified**

The Trustee and the Methodist Council have agreed that any funding shortfalls identified at an actuarial valuation should be eliminated by the payment of additional contributions over the recovery period. The level and period over which these additional contributions are to be paid will be agreed between the Trustee and the Conference. In determining the actual recovery period at any particular valuation the Trustee’s principles are to take into account the following factors:

* the Rules of the Scheme;
* the size of the funding shortfall;
* the business plans of the Methodist Church;
* the Trustee’s assessment of the financial covenant of the Methodist Church; and
* any contingent security offered by the Methodist Church.

The assumptions to be used in these calculations will be those set out above for calculating the technical provisions except that they may also take account of some of the expected investment out-performance of Scheme assets over the discount rates used to calculate the technical provisions, as agreed by the Trustee and the Methodist Council, depending upon the circumstances at the time.

For the 1 September 2014 valuation, it has been assumed that the assets will achieve a return of 4.7% pa over the recovery plan length.

1. **Policy on reduction of cash equivalent transfer values (CETVs)**

The Trustee will ask the actuary to advise them at each valuation of the extent to which assets are sufficient to provide CETVs for all non pensioners without adversely affecting the security of the benefits of other members and beneficiaries. Where coverage is less than 100% of benefits in excess of the first priority slice (broadly those benefits which would be provided were the Scheme to be admitted to the Pension Protection Fund), the Trustee may consider whether CETVs should be reduced as permitted under legislation, after obtaining actuarial advice as to the appropriate extent.

If at any other time, after obtaining advice from the actuary, the Trustee is of the opinion that the payment of CETVs at a previously agreed level may adversely affect the security of the benefits of other members and beneficiaries, the Trustee will commission a report from the actuary and will use the above criterion to decide whether, and to what extent, CETVs should be reduced.

1. **Payments to the Methodist Church**

Payments to the Methodist Church are not permitted under the rules of the Scheme unless the Scheme is being wound up and all of the benefits have been provided for.

1. **Frequency of valuations and circumstances for extra valuations**

This actuarial valuation under Part 3 of the Pensions Act 2004 is being carried out as at the effective date of 1 September 2014 and subsequent valuations will, in normal circumstances, be carried out every three years thereafter. An actuarial report on developments affecting the Scheme’s funding level will be obtained as at each intermediate anniversary of that date.

The Trustee may call for a full actuarial valuation instead of an actuarial report when, after considering the actuary’s advice, they are of the opinion that events have made it unsafe to continue to rely on the results of the previous valuation as the basis for future contributions. However, the Trustee will consult the Methodist Council before doing so.

1. **Interaction with investment strategy**

The assets that most closely match the Scheme’s liabilities are index-linked and fixed-interest gilts of appropriate term compared to the liabilities. The Scheme is partly invested in assets such as equities that are expected, although not guaranteed, to produce a higher return than gilts over the long term. The Scheme has a significant mis-matched position of its assets and liabilities. The SRC has confirmed that it is comfortable with this position which is supported by the strong covenant of the Church. The Trustee understands that this mis-matched position could lead to a volatile funding position. The Trustee further understands that investing in equities is expected to reduce the expected contributions required from the Church in the long run.

An allowance for part of the extra return expected from equity investment has been taken into account in setting the Scheme’s technical provisions and in calculating the contributions required under the recovery plan. If this extra return is not achieved, the shortfall will ultimately need to be met by increased contributions from the Church. Both the Church and the Trustee appreciates that the contributions required can be volatile.

The Trustee regularly reviews the Scheme’s investment strategy taking into account the funding position and liability profile. The Trustee will consult fully with the Methodist Council before any changes are made to the investment strategy.

1. **Risks**

The Trustee and the Church recognise that there are a number of risks inherent in the funding plan and that additional funding may be required at future valuations if the experience of the Scheme is not in line with the assumptions made. In addition to the investment risk detailed above, there is also longevity risk. Future improvements in life expectancy may be greater than anticipated. In setting the Scheme’s funding target, mortality assumptions are made based on wider population statistics and adjusted to make some allowance for future improvements in longevity. The mortality assumptions are reviewed at each formal triennial actuarial valuation.

**This statement has been agreed by the Methodist Council on behalf of Conference:**

Signed on behalf of the Methodist Council

Name:

Position:

Date:

**This statement was agreed by the Trustee at their meeting on 5 March 2015:**

Signed on behalf of the Trustee of the Methodist Ministers’ Pension Scheme

Name:

Position: Trustee

Date:

**This statement has been agreed by the Trustee after obtaining actuarial advice from me:**

Signed:

Name: Stephen Ainsworth, FIA

Position: Actuary to the Methodist Ministers’ Pension Scheme

Date:

**APPENDIX 1**

**Current investment strategy of the Methodist Ministers’ Pension Scheme**

The long term target asset allocation is currently as follows:

|  |  |
| --- | --- |
| Benchmark asset allocation | Long term benchmark asset allocation  % |
| Equity investment | 58 |
| Bond investment | 34 |
| Property investment | 8 |
| Cash | 0 |

**APPENDIX 2**

**Economic assumptions as at the valuation date**

|  |  |
| --- | --- |
| **Valuation date** | **1 September 2014** |

**Discount rate**

The discount rate used to value the liabilities (before adjustments) is determined as the annual nominal spot rate provided by the Bank of England as at the valuation date, calculated at the mean duration of the Scheme’s liabilities.

**Inflation**

The RPI inflation assumption is derived as the annual inflation spot rate provided by the Bank of England as at the valuation date, calculated at the mean duration of the Scheme’s liabilities. The CPI inflation assumption is derived as the RPI assumption less 0.7%.

**Market conditions at the valuation date**

|  |  |
| --- | --- |
| Annualised yields on 31 August 2014 |  |
| Duration of Scheme’s liabilities | 13 years |
| Annual nominal gilt yield spot rate provided by the Bank of England at 13 years duration | 2.7% |
| Annual inflation spot rate provided by the Bank of England at 13 years duration | 3.2% |

**Economic assumptions**

|  |  |
| --- | --- |
| Type of assumption | % pa |
| Pre-retirement outperformance assumption | 2.0 |
| Post retirement outperformance assumption | 1.0 |
| Pre-retirement discount rate | 4.7 |
| Post retirement discount rate | 3.7 |
| Inflation – RPI | 3.2 |
| Inflation – CPI | 2.5 |
| Stipend increase adjustment | 0.75 |
| Stipend increases | 3.25 |
| Pension increases  Service to September 2006  Service from September 2006 | 3.1  2.1 |
| Deferred pension increases |  |
| Service to April 2009 | 2.5 |
| Service from April 2009 | 2.5 |
| Management expenses (as a percentage of stipends) | 2.3 |

**APPENDIX 3**

**Demographic assumptions as at the valuation date**

**Illustrative death rates**

Mortality prior to retirement: probability of death within one year

|  |  |  |
| --- | --- | --- |
| Age  x | Male death rate qx  AMC00 | Female death rate qx  AFC00 |
| 20 | 0.000464 | 0.000194 |
| 25 | 0.000485 | 0.000230 |
| 30 | 0.000531 | 0.000295 |
| 35 | 0.000626 | 0.000408 |
| 40 | 0.000820 | 0.000604 |
| 45 | 0.001208 | 0.000949 |
| 50 | 0.001963 | 0.001550 |
| 55 | 0.003400 | 0.002600 |
| 60 | 0.006064 | 0.004433 |
| 65 | 0.010875 | 0.007628 |

Mortality in retirement (normal health): probability of death within one year

|  |  |  |  |
| --- | --- | --- | --- |
| Age  X | Male death rate qx  SAPS S2 series light tables with CMI 2013 projections, with a long term rate of improvement in mortality rates of 1.5% pa, with a scaling factor of 95% | Female death rate qx  SAPS S2 series light tables with CMI 2013 projections, with a long term rate of improvement in mortality rates of 1.5% pa, with a scaling factor of 95% | Widow death rate qx  SAPS S2 series light tables with CMI 2013 projections, with a long term rate of improvement in mortality rates of 1.5% pa, with a scaling factor of 87.5% |
| 60 | 0.003630 | 0.004241 | 0.003906 |
| 65 | 0.005334 | 0.005455 | 0.005025 |
| 70 | 0.009500 | 0.008572 | 0.007895 |
| 75 | 0.017650 | 0.015299 | 0.014091 |
| 80 | 0.032998 | 0.028920 | 0.026636 |
| 85 | 0.066630 | 0.058964 | 0.054309 |
| 90 | 0.134705 | 0.113233 | 0.104294 |
| 95 | 0.235755 | 0.190479 | 0.175441 |
| 100 | 0.343775 | 0.292395 | 0.269311 |
| 105 | 0.435793 | 0.396689 | 0.365372 |

Life expectancy implied by the tables for a person currently aged 65 is 24.2 years for a male and 25.3 years for a female. Life expectancy implied by the tables for a person currently aged 45 at age 65 is 26.2 years for a male and 27.6 years for a female.

**Illustrative retirement rates**

|  |  |  |
| --- | --- | --- |
| Probability of retiring within one year | | |
| Age X | Normal health Rx | Ill health Ix |
| NPD - 35 | 0 | 0.002 |
| NPD - 25 | 0 | 0.002 |
| NPD - 15 | 0 | 0.004 |
| NPD - 5 | 0 | 0.01 |
| NPD - 4 | 0 | 0.01 |
| NPD - 3 | 0 | 0.01 |
| NPD - 2 | 0 | 0.01 |
| NPD - 1 | 0.19 | 0.01 |
| NPD | 1 | 0 |

**Age difference of dependants**

Actual age difference is used for pensioners where the data is available. Where the data is unknown, and for all active and deferred members, male members are assumed to be, on average, two years older than their spouses or civil partners and female members two years younger than their spouses or civil partners.

**Percentage of members with spouse/dependant benefits**

Actives and deferreds: 90% of male members and 75% of female members are assumed to have spouse/dependants benefits at retirement or earlier death

Pensioners: Based on actual marital/dependency status, where known, otherwise the same proportions as above.

**Commutation**

Active and deferred members commute 15% of their main Scheme benefits on retirement for a lump sum.

**Normal Pension Date (NPD)**

For pensionable service prior to 1 September 2013 NPD has been taken as 31 August in the calendar year of attaining age 65. For pensionable service from 1 September 2013, NPD has been taken as 31 August in the calendar year of attaining the male State Pension Age (SPA). The male SPA has been taken as age 65 rising to age 66 by October 2020, rising to age 67 by 2028 and rising to age 68 by 2046. It is possible that the Government will being forward the rise to age 68 but no allowance has been made for this in the calculations because the changes are just proposals at this stage.

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**METHODIST MINISTERS’ PENSION SCHEME**

**Recovery Plan**

Introduction

The recovery plan agreed by the Trustee on 1 March 2012 has been reviewed and revised by the Trustee to satisfy the requirements of Section 226 of the Pensions Act 2004, after obtaining the advice of Stephen Ainsworth, the Scheme Actuary, and after obtaining the agreement of the Conference of the Methodist Church.

This recovery plan follows the actuarial valuation of the Scheme as at 1 September 2014, which revealed a funding shortfall (technical provisions minus value of assets) of £40.0m.

**Steps to be taken to ensure that the Statutory Funding Objective is met**

To eliminate this funding shortfall, the Trustee and the Conference of the Methodist Church have agreed that additional contributions (ie contributions over and above those needed to cover benefits being earned in the future) will be paid to the Scheme by persons responsible for providing a Current Member’s remuneration of:

9.8% of Stipends each month until the funding shortfall is eliminated.

In addition fixed contributions of £1m per annum will continue to be transferred to the Scheme from the Pension Reserve Fund during each September from September 2015 until the shortfall is eliminated.

**Period in which the Statutory Funding Objective should be met**

Under this recovery plan, if the assumptions made are borne out in practice the total funding shortfall will be eliminated in 6 years 4 months from the valuation date 1 September 2014, which is by 31 December 2020. The assumptions are:

* technical provisions will continue to be calculated according to the method and assumptions set out in the statement of funding principles agreed by the Trustee at their meeting on 5 March 2015, with financial conditions unchanged from those at the valuation effective date;
* Scheme experience will be in line with the assumptions underlying the technical provisions;
* the return on assets over the period of the recovery plan will be 4.7% pa;
* the Scheme will remain open to new members and the shortfall reduction contributions will also be paid in respect of these new members.

**Progress towards meeting the Statutory Funding Objective**

On the assumptions made, 50% of the above additional contributions will be paid in 3 years 3 months, which is by 30 November 2017.

This recovery plan was agreed by the Trustee at their meeting on 5 March 2015, to be effective from 1 September 2015.

Signed on behalf of the Trustee of the Methodist Ministers’ Pension Scheme

Name

Position

Date

Signed on behalf of the Methodist Conference

Name

Position

Date



