

Pension and Assurance Scheme for Lay Employees of the Methodist Church (PASLEMC) Valuation Results

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Status of paper	Draft
Action Required	Decision
Draft Resolutions	At end of the report.
Alternative Options to Consider, if Any	If the SRC or Council wished to consider other options further discussions would be necessary with the Pension Board

Summary of Content

Subject and Aims	To note the results of the triennial valuation for PASLEMC and confirm the basis of the assumptions agreed between the Trustee Board and the Finance Sub-Committee (FSC) of the SRC and the ongoing contributions to the Scheme.
Main Points	The triennial valuation has been concluded and the Trustees have discussed and agreed the basis for the assumptions with the FSC. PASLEMC is showing a lower deficit in the fund at this valuation although there has been a significant increase in the cost of providing future service benefits. Employer contributions would have to increase unless there was an increase in member contributions or a reduction in future service benefits. The paper recommends that the Council agree to consult with members to reduce the future service benefits by linking the normal retirement date to the male State Pension date for service from 1 September 2015.
Background Context and Relevant Documents	The paper follows agreement between the Trustee Board and the FSC and follows the presentation to the Methodist Council in January 2015. The FSC recommendations were agreed by the Strategy and Resources Committee.

Summary of Impact

Financial	The employer contribution rate would increase if no action was taken.
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Pension and Assurance Scheme for Lay Employees of the Methodist Church (PASLEMC) Valuation Results

Introduction

1. The valuation results for PASLEMC have been based on the actuarial basis which has been agreed between the Trustee and the Finance Sub-committee (FSC) of the Strategy and Resources Committee.
2. It has been agreed that the Methodist Council will make the decisions required on scheme funding issues on behalf of all the employers that participate in the Scheme for PASLEMC, other than the Central Finance Board who participated in the discussions to agree the actuarial basis.
3. The actuarial valuation is essentially a planning exercise. The output is a level of contributions that is considered likely to be sufficient to meet the future liabilities of the Scheme and, where a shortfall exists, the contributions that are required to meet the funding target.
4. The technical provisions of the Scheme (the past service liabilities) are derived by projecting forward benefit cash flows, for up to 80 years or so, and discounting these to the valuation date with an allowance for anticipated investment returns that are believed to be prudent. This is different to an economic valuation or the price that would need to be paid to secure the liabilities with a third party, both of which would result in higher values.
5. The results of the valuation have revealed a reduction in the shortfall from £2.2m in 2011 to £0.3m in 2014, however there was a significant increase in the total future service contribution rate from 27.8% of pensionable salaries in 2011 to 33.9% of pensionable salaries on the proposed basis for 2014. The increase in the future service contribution rate is mainly due to the fall in bond yields.
6. The employer future service contribution rate would increase to 25.9% of pensionable salaries if the member contribution rate was maintained at the current rate of 8% of pensionable salaries. The current employer contribution rate, including 4.3% shortfall contributions, is 24.1% of pensionable salaries.
7. The Strategy and Resources Committee recommends that the Council will propose to the Conference as part of the Connexional Central Services Budget for 2015/16 that the shortfall of £0.3m (£0.45m by 1 September 2015) be paid as a one-off payment from the Pension Reserve Fund. The Strategy and Resources Committee also recommends that the Council agrees to consult with active members to reduce the future service benefits by linking the normal pension date to the male State Pension date for service from 1 September 2015.

The employers' covenants

8. As part of the consideration of the preliminary valuation results, the Trustee must have regard to the strength of the covenant of the Methodist Council and also that of the other participating employers in respect of PASLEMC.
9. The Trustee had extensive discussions with the FSC and a comprehensive review of the covenant of the Methodist Council has been provided to enable the Trustee to assess the strength of that covenant. Other participating employers have responded individually to questions raised regarding the strength of their covenants.

10. The strength of the covenant of the Methodist Council and the strength of the other participating employers' covenants will help determine how prudent the actuarial assumptions need be. The Trustee has assessed the strength of the covenant of the Methodist Council as strong. The strengths of the covenants of the other participating employers have been assessed as not as strong as the Methodist Council although some participating employers have significant assets.

Prudent assumptions

11. Funding assumptions need to be made about the likely course of events.
12. The regulations require that the assumptions overall are chosen prudently. By prudent, the regulations require assumptions which, if the Scheme continues on an ongoing basis, are more likely to overstate than understate the amount of money actually required to meet the cost of the benefits.
13. In particular, the Pensions Regulator expects prudent assumptions to be used for the discount rate and mortality rate used in the calculations.

Assumptions

14. The valuation results have been produced using a set of actuarial assumptions which the Trustee Board has agreed with the FSC.

Assumption	Proposed basis for 2014 valuation	Any change from 2011 valuation basis
Pre Retirement Discount Rate	Gilts + 2.0% = 5.0%	Updated to reflect current market conditions
Post Retirement Discount Rate	Gilts + 0.5% = 3.5%	Updated to reflect current market conditions
Pensionable Earnings Increases	CPI + 1% + Scale = 3.7% + scale	Updated to reflect current market conditions
Pension Increases	As guaranteed in the Rules, based on RPI increases	Updated to reflect current market conditions
Commutation	An allowance for members to commute 15% of their pensions for a lump sum	A change from no allowance
Mortality	Most up to date tables and improvement factors	A change to using the most up to date tables
Expenses	3.7%	An increase from 3.5% to reflect increased regulatory fees

15. A copy of the Statement of Funding Principles agreed by the Trustees which will require signature on behalf of the Methodist Council is attached to this paper.

Assets

16. The assets of the Scheme had a market value of £51.08m as at 31 August 2014. On the valuation basis the Scheme was 99.4% funded as at 1 September 2014.

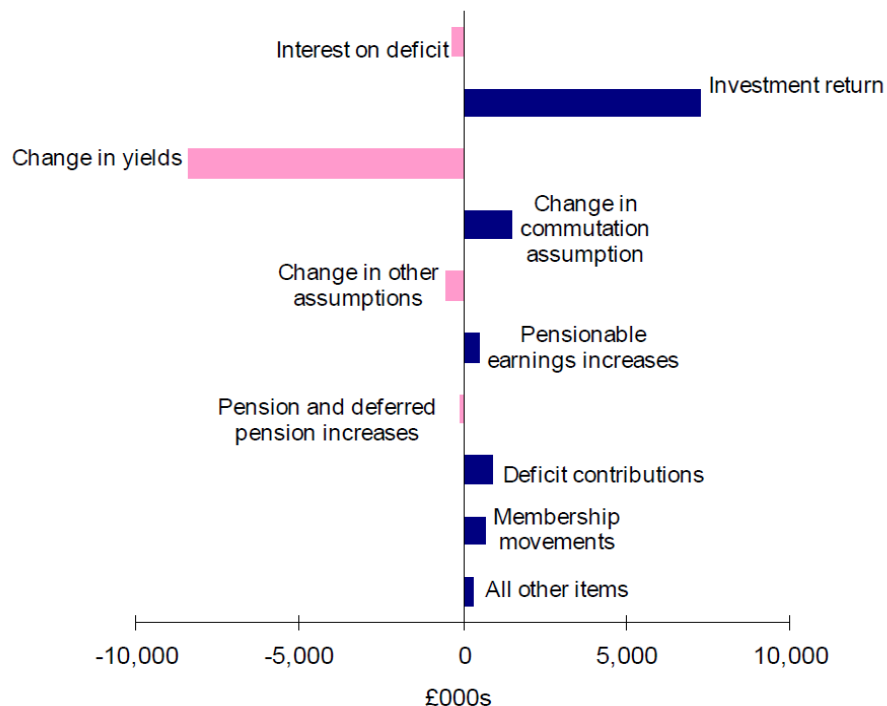
Results

17. The results of the actuarial valuation compared to the previous valuation in 2011:

	2014	2011
Technical provisions (liabilities)	£51.39m	£37.59m
Market value of assets	£51.08m	£35.43m
Past service shortfall (£'m)	£0.31m	£2.16m
Funding ratio	99.4%	94.3%
Total future service contribution rate (% pensionable earnings)	33.9%	27.8%

Change in funding position

18. The valuation carried out as at 1 September 2011 revealed a shortfall of £2.2m. The position has improved and the graph below shows the main factors to the change in funding level position over the three years to 1 September 2014:



19. Although the change in yields had significantly increased the value placed on the liabilities under the Scheme, this was in the main offset by the good investment return. In addition the change in the commutation assumption and the deficit contributions helped reduce the shortfall to £0.3m.

Membership

20. The Membership profile as at 31 August 2014 is shown in the table below. For comparison, figures as at 31 August 2011 are shown in brackets.

Active	197	(208)
Deferred	247	(206)
Pensioners	<u>173</u>	<u>(134)</u>
Total	617	(548)

Recovery plan

The requirements

21. The valuation results have revealed a small shortfall and the recovery plan to eliminate this shortfall will need to be agreed with the Methodist Council.

Existing recovery plan

22. At the previous valuation, a shortfall of £2.2m was revealed. The current contributions being paid to eliminate this shortfall are contributions of 4.3% of pensionable earnings to 29 February 2020.
23. The Finance Sub-Committee recommends that the Council agrees to recommend to the Conference that the shortfall be met by a one-off payment from the Pension Reserve Fund. The payment required on 1 September 2015 would be £448,000, which represents the shortfall at 1 September 2014 together with interest and the additional shortfall that will arise in 2014/15 due to contributions being below the future service rate. If the Conference do not agree to the payment from the Pension Reserve Fund the Trustee will expect the Employers to pay additional contributions of 1.5% per annum so that there was no change to the expected end of the recovery plan.
24. If the shortfall was eliminated by the payment of a lump sum from the Pension Reserve Fund, the only contributions required would be those in relation to the funding of future service benefits.

Contributions and benefits from 1 September 2015

25. The FSC was advised by the Trustee Board that the employer contribution would have to increase unless member contributions increase or the benefit structure is amended.
26. The employer contribution needed to provide for future service benefits is 25.9% of pensionable earnings, with the employers currently paying 24.1% (if the member contribution remains at 8% of pensionable salaries).
27. The FSC explored various ways that the benefit structure could change to ensure that the employer contribution rate was kept at or below 24.1% of pensionable salaries. A change to link the normal pension date to the male State Pension date would reduce the future service contribution rate by 2.2%. This is the equivalent change to that made for the Methodist Ministers Pension Scheme (MMPS) in 2013.
28. The Strategy and Resources Committee recommend that the Methodist Council agree to consult with members to link the normal pension date to the male State Pension date for pensionable service after 1 September 2015. For service to 31 August 2015 the normal pension date would remain at 65.
29. The Methodist Council will need to delegate the final decision on the benefits change which needs to be implemented from 1 September 2015. It is proposed that the Council appoints two of its members, plus the Finance Sub Committee of the SRC, to consider the response to the consultation and agree the resultant action.
30. The Strategy and Resources Committee recommends that the employer contribution rate remains at 24.1% of pensionable salaries from 1 September 2015 if the benefit change is agreed. If the benefit change is not agreed the Trustee will expect the employers to pay contributions for future service benefits of 25.9% of pensionable earnings.

Pensionable Earnings from 6 April 2016

31. The Scheme's current pensionable salary definition is "a Member's basic annual earnings on 1 September each year reduced by an amount equal to the basic flat-rate annual retirement pension for a single person under the State Scheme." From 6 April 2016 the basic flat-rate state pension will be replaced by the single-tier state pension. The current basic flat-rate state pension is £113.10 per week (£5,881.20 per annum) and the current single-tier state pension is £148.40 per week (£7,716.80 per annum).
32. As a consequence of the change to state pensions the pensionable salaries for all active members of PASLEMC will drop by around £1,800 per annum, resulting in immediate lower accrued pensions from 1 September 2016.
33. The table below shows the impact on accrued pension for a low earner and a high earner with either 10 years or 20 years pensionable service:-

	Lower Earner – current Basic Salary £25,000 per annum		Higher Earner – current Basic salary £50,000 per annum	
Pensionable Service	Accrued pension on 1.9.2016 before state pension change	Accrued pension on 1.9.2016 after state pension change	Accrued pension on 1.9.2016 before state pension change	Accrued pension on 1.9.2016 after state pension change
10 years	£2,731 p.a.	£2,469 p.a.	£6,302 p.a.	£6,040 p.a.
20 years	£5,917 p.a.	£5,349 p.a.	£13,655 p.a.	£13,087 p.a.

34. Any change to the definition of pensionable salary will require a consultation with members irrespective of whether it would increase or decrease the value of members' benefits.
35. The Council has two main options:-
- To do nothing. If the Council decides not to consult with members to amend the definition of pensionable salaries then the accrued pensions for all active members will fall on 1 September 2016. In this situation the funding of the pension scheme will improve because active members' accrued pension will reduce in value. The actuary to the Trustee Board has not calculated the impact on the funding position but has advised it would fairly 'substantial'.
 - To consult with members to amend the definition of pensionable salary replacing the current basic flat-rate state pension with a percentage of the single-tier state pension that is roughly equal in value. There would be no impact to the funding position
36. The current Basic rate State Pension is 76.212% of the flat-rate pension. It would be recommended that the Council consult with members to amend the definition of pensionable salary to 'basic earnings less 75% of the flat-rate pension'. This would give members very slightly more accrued pension but will be a simpler definition for members to understand going forward.
37. If the Methodist Council agreed to consult with members to protect their accrued pension then the consultation can be included with the proposed change to link the normal pension date to the male state pension age. The responses to the consultation on the proposed amendment to the definition of pensionable salary can be considered at the October Council meeting. If agree the amendment would become effective from 6 April 2016.

Solvency position

38. The Actuaries also reviewed the position if the Scheme were discontinued on the valuation date with all members treated as having left service and the Scheme assets used to buy immediate and deferred annuities from an insurance company.
39. The solvency estimate provides an indication of the extent to which the Trustee is reliant on the employers to stand behind the Scheme.
40. The solvency position as at 1 September 2014 and compared to 1 September 2011 is as follows:

	2014	2011
Shortfall	£18m	£18.7m
Funding level	73.9%	65%

Next Steps

41. To finalise the valuation a formal report will be produced by the Actuary together with other documentation, detailed below, which will require signature on behalf of the Methodist Council.
- Statement of Funding Principles
 - Recovery plan
 - Schedule of contributions (to be signed after conclusion of the consultation with members on the change to link the normal pension date to the male State Pension date)
42. A copy of the Statement of Funding Principles, the Recovery Plan and the Schedule of Contributions are attached to this paper.

***RESOLUTIONS

- 31/1. The Methodist Council agrees to the Statement of Funding Principles, including the economic and demographic assumptions proposed by the Trustee of PASLEMC as the basis of the Actuarial Valuation and authorises it to be signed on its behalf.**
- 31/2. The Methodist Council agrees to the Recovery Plan and authorises this to be signed on its behalf.**
- 31/3. The Methodist Council agrees to consult with members in May and June 2015 with regard to linking the normal retirement date to the male State Pension date for service from 1 September 2015.**
- 31/4. The Methodist Council agrees to the Schedule of Contributions.**
- 31/5. The Council agrees to consult with members in May and June 2015 with regard to amending the definition of pensionable salary to change from the current deduction of Basic State Pension to 75% of the new single-tier State Pension from 6 April 2016.**
- 31/6. The Methodist Council delegates the final consideration and decision on the benefits change which needs to be implemented from 1 September 2015 to the Finance Subcommittee of the Strategy and Resources Committee which for the purposes of considering this matter shall be supplemented by two members of the Council.**