***MC/15/31***

**Draft**

**PENSION AND ASSURANCE SCHEME FOR LAY EMPLOYEES OF THE METHODIST CHURCH**

**Statement of Funding Principles**

# 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 Diana Simon, the actuary to the Scheme and after consulting with the Central Finance Board and the Finance Sub Group of the Strategy and Resources Committee (“SRC”) of the Methodist Church on behalf of the Methodist Council and the other participating employers of the Scheme (“the Employers”).

# 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.

# Funding objectives in addition to the statutory funding objective

None

# 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.

## 4.3 Method

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

## 4.4 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.

## 4.5 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 Employers’ covenants and market conditions at the time of the valuation. The premiums at 1 September 2014 are 2% pa pre retirement and 0.5% 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 markets expectation 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 6 April 2005 and capped at 2.5% pa for benefits accrued on or after 6 April 2005. Pensions which accrued prior to 1 September 1998 for members who joined the Scheme prior to 1 December 1997 increase at 5% pa. 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.
* **Pensionable Earnings increases:** Pensionable Earnings are assumed to increase at the rate of CPI inflation plus a salary increase adjustment together with an age related scale to allow for promotional increases. Sample rates are included in Appendix 3 to this statement. The adjustment is 1% 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. 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.
* **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:** Allowance has been made for withdrawals from service prior to Normal Retiring Dates by means of an age related scale. Sample rates are included in Appendix 3 to this statement.
* **Retirement:** Members who joined the Scheme prior to 1 December 1997 are assumed to retire at age 62 other than female members who did not elect for a pension age of 65 in 1991 who are assumed to retire at age 60. All other members are assumed to retire at age 65. Deferred members are assumed to start to receive their pensions at the earliest age they can do so unreduced. 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.

# Employer contributions

The contributions payable by the Employers 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.

# 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 the Methodist Council.

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.

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

The Trustee, the Central Finance Board 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, the Methodist Council (representing all the participating employers other than the Central Finance Board) and the Central Finance Board. 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 and the other participating employers;
* the Trustee’s assessment of the financial covenant of the Methodist Church and the other participating employers; and
* any contingent security offered by the Methodist Church or the other participating employers.

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, the Methodist Council and the Central Finance Board, depending upon the circumstances at the time.

For the 1 September 2014 valuation, it has been assumed that no additional investment outperformance other than that allowed for in the discount rates will be earned on the Scheme’s assets.

# 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.

# Payments to the Employers

Payments to the Employers 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.

# 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 and the Central Finance Board before doing so.

# 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 Trustee understands that investing in equities is expected to reduce the expected contributions required from the Employers 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 Employers. Both the Methodist Council, the Central Finance Board and the other participating employers 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.

# Risks

The Trustee, the Methodist Council, the Central Finance Board and the other participating employers 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 the 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 as part of formal triennial actuarial valuations.

**This statement has been agreed by the Central Finance Board and the Methodist Council on behalf of the participating employers other than the Central Finance Board:**

Signed on behalf of the Methodist Council

Name:

Position:

Date:

Signed on behalf of the Central Finance Board

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 Pension and Assurance Scheme for Lay Employees of the Methodist Church

Name:

Position: Trustee

Date:

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

Signed:

Name: Diana Simon, FIA

Position: Actuary to the Pension and Assurance Scheme for Lay Employees of the Methodist Church

Date:

**APPENDIX 1**

**Current investment strategy**

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 | 19 years |
| Annual nominal gilt yield spot rate provided by the Bank of England at 19 years duration | 3.0% |
| Annual inflation spot rate provided by the Bank of England at 19 years duration | 3.4% |

**Economic assumptions**

|  |  |
| --- | --- |
| Type of assumption | % pa |
| Pre-retirement outperformance assumption | 2.0 |
| Post retirement outperformance assumption | 0.5 |
| Pre-retirement discount rate | 5.0 |
| Post retirement discount rate | 3.5 |
| Inflation RPI | 3.4 |
| Inflation CPI | 2.7 |
| Pensionable Earnings increase adjustment | 1.0 |
| Pensionable Earnings increases | 3.7 |
| Pension increases 5% fixed 5% LPI 2.5% LPI | 5.03.22.2 |
| Deferred pension increases |  |
|  Service to April 2009 | 2.7 |
|  Service from April 2009 | 2.5 |
| Management expenses (as a percentage of Pensionable Earnings) | 3.7 |

**APPENDIX 3**

**Demographic assumptions as at the valuation date**

**Illustrative death rates**

Mortality prior to retirement: probability of death within one year

|  |  |  |
| --- | --- | --- |
| Agex | Male death rate qxAMC00 | Female death rate qxAFC00 |
| 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

|  |  |  |
| --- | --- | --- |
| Agex | Male death rate qxSAPS 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 100% | Female death rate qxSAPS 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 100% |
| 60 | 0.003821 | 0.004464 |
| 65 | 0.005615 | 0.005742 |
| 70 | 0.010000 | 0.009023 |
| 75 | 0.018579 | 0.016104 |
| 80 | 0.034734 | 0.030442 |
| 85 | 0.070136 | 0.062068 |
| 90 | 0.141795 | 0.119193 |
| 95 | 0.248163 | 0.200504 |
| 100 | 0.361868 | 0.307784 |
| 105 | 0.458729 | 0.417568 |

Life expectancy implied by the tables for a person currently aged 65 is 23.8 years for a male and 24.9 years for a female. Life expectancy implied by the tables for a person currently aged 45 at age 65 is 25.8 years for a male and 27.1 years for a female.

**Illustrative promotional salary scale**

|  |  |
| --- | --- |
| Agex | Promotional salary scale |
| 20 |  44 |
| 30 |  64 |
| 40 |  79 |
| 50 |  93 |
| 60 |  103 |

**Illustrative withdrawal rates**

|  |
| --- |
| Withdrawal from service |
| Agex | Percentage leaving the Scheme within 1 year |
| 20 | 11 |
| 30 | 6 |
| 40 | 4 |
| 50 | 0 |
| 60 | 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 two years older than their spouses or civil partners and females two years younger than their spouses or civil partners.

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

Actives and Deferreds: 85% 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

**Commutation**

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

|  |
| --- |
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**PENSION AND ASSURANCE SCHEME FOR LAY EMPLOYEES OF THE METHODIST CHURCH**

**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 Diana Simon, the Scheme Actuary, and after obtaining the agreement of the Employers namely:

|  |  |  |
| --- | --- | --- |
| The Methodist CouncilCliff CollegeCentral Finance BoardMethodist Ministers’ Housing SocietyCentral Hall Westminster Limited |  | Wesley College, CambridgeGuy Chester CentreTrustees for Methodist Church PurposesMethodist Relief and Development Fund |

It follows the actuarial valuation of the Scheme as at 1 September 2014, which revealed a funding shortfall (technical provisions minus value of assets) of £311,000.

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

To eliminate this funding shortfall, the Trustee and the Employers have agreed that an additional contribution (ie a contribution over and above those needed to cover benefits being earned in the future) will be paid to the Scheme as follows:

A lump sum payment of £448,000 will be transferred from the Pension Reserve Fund to the Scheme in September 2015. This represents the funding shortfall at 1 September 2014 together with interest until the date of payment of the lump sum (£324,000) and the additional expected shortfall that will arise in the 2014/15 Scheme year due to contributions being paid below the future service rate (£124,000).

**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 is expected to be eliminated in September 2015 which is 1 year 1 month after the valuation date of 1 September 2014. 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.

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 Pension and Assurance Scheme for Lay Employees of the Methodist Church

Name

Position

Date

Signed on behalf of The Methodist Council

Name

Position

Date

Signed on behalf of Cliff College

Name

Position

Date

Signed on behalf of Central Finance Board

Name

Position

Date

Signed on behalf of Methodist Ministers’ Housing Society

Name

Position

Date

Signed on behalf of Central Hall Westminster Limited

Name

Position

Date

Signed on behalf of Wesley College, Cambridge

Name

Position

Date

Signed on behalf of Guy Chester Centre

Name

Position

Date

Signed on behalf of Trustees for Methodist Church Purposes

Name

Position

Date

Signed on behalf of Methodist Relief and Development Fund

Name

Position

Date

|  |
| --- |
| **DRAFT** |

**PENSION AND ASSURANCE SCHEME FOR LAY EMPLOYEES OF THE METHODIST CHURCH**

**Schedule of Contributions for the period 1 September 2015 to 31 August 2020**

The schedule of contributions agreed by the Trustee on 1 March 2012 has been reviewed and revised by the Trustee to satisfy the requirements of Section 227 of the Pensions Act 2004, after obtaining the advice of Diana Simon, the Scheme Actuary and after obtaining the agreement of the Employers, namely:

|  |  |  |
| --- | --- | --- |
| The Methodist CouncilCliff CollegeCentral Finance BoardMethodist Ministers’ Housing SocietyCentral Hall Westminster Limited |  | Wesley College, CambridgeGuy Chester CentreTrustees for Methodist Church PurposesMethodist Relief and Development Fund |

It covers contributions to the Scheme from all Employers who participate in the Scheme from time to time.

1. **Employer contributions**

 In respect of future accrual of benefits, the provision of death in service benefits and the expenses of administering the Scheme, each Employer will pay the following:

* 24.1% pa of pensionable earnings from 1 September 2015.

 These contributions are to be paid to the Scheme on or before the 19th day of the calendar month following that to which the payment relates.

In respect of the shortfall in funding in accordance with the recovery plan agreed by the Trustee on 5 March 2015, a lump sum payment of £448,000 will be transferred from the Pension Reserve Fund to the Scheme in September 2015.

1. **Expenses**

These contributions include 3.7% pa of pensionable earnings in respect of expenses, including an annual provision of £23,300 pa for payment of the regulatory fees including the Pension Protection Fund levy.

1. **Augmentation payments**

 In respect of any augmentations granted, the relevant Employer will pay additional amounts to cover the costs of benefit augmentations within one month of the later of the date of granting the augmentation and the date on which the Trustee receives the details of the costs from the Scheme Actuary.

1. **Contributions by active members**

Members will pay contributions at the rate of 8% pa of pensionable earnings.

These contributions are to be deducted from pay by the Employers and paid to the Scheme on or before the 19th day of the calendar month following deduction.

 These amounts do not include members’ Additional Voluntary Contributions.

1. **Definition of Pensionable Earnings**

 The definition of pensionable earnings is the rate of 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.

Signed on behalf of the Trustee of the Pension and Assurance Scheme for Lay Employees of the Methodist Church

Name

Position

Date

Signed on behalf of The Methodist Council

Name

Position

Date

Signed on behalf of Cliff College

Name

Position

Date

Signed on behalf of Central Finance Board

Name

Position

Date

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Position

Date

Signed on behalf of Guy Chester Centre

Name

Position

Date

Signed on behalf of Trustees for Methodist Church Purposes

Name

Position

Date

Signed on behalf of Methodist Relief and Development Fund

Name

Position

Date