

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

<b>Contact Name and Details</b>	Meena Tooray – Pensions Manager tooraym@methodistchurch.org.uk
<b>Resolutions</b>	<p>75/1. The Council receives the report and notes the final results of the 2017 actuarial valuation.</p> <p>75/2. The Council notes the update on the consultation with Scheme members regarding future benefits within the Pensions and Assurance Scheme for Lay Employees of the Methodist Church and the anticipated timetable for consideration of the responses.</p> <p>75/3. The Council notes the rule change in respect of de minimus payments up to £10,000.</p> <p>75/4. The Council notes that the Deed of Amendment clarifies the position and brings in reference to payments prescribed by regulation.</p>

### Summary of Content and Impact

<b>Subject and Aims</b>	<ul style="list-style-type: none"> <li>To note the results of the triennial valuation for PASLEMC and progress on the consultation with members regarding the future of PASLEMC.</li> </ul>
<b>Main Points</b>	<ul style="list-style-type: none"> <li>The triennial valuation has been concluded and the Trustee has discussed and agreed the basis for the assumptions with the Finance Sub-committee (FSC) and the other participating employers.</li> <li>PASLEMC is showing a higher deficit at this valuation which the Conference has agreed will be met by lump sum payments from the Pension Reserve Fund over five years commencing in August 2018.</li> <li>The cost of accrual increased with effect from 1 September 2017 but contribution rates currently remain unchanged because the cost of the future service shortfall arising between 1 September 2017 and 31 August 2019 is included within the Pension Reserve Fund contributions.</li> <li>The future of the Scheme is currently under review and a statutory consultation with Scheme members is taking place. Should the current structure be retained, and member contribution levels be unchanged, the Employer contributions would have to increase from 1 September 2019.</li> </ul>
<b>Background context</b>	<ul style="list-style-type: none"> <li>The paper follows agreement between the Trustee Board and the FSC and the other participating employers.</li> </ul>

## Introduction

1. The valuation results for PASLEMC have been based on the actuarial basis which has been agreed between the Trustee and the FSC and the other participating employers.
2. 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.
3. The technical provisions of the Scheme (the past service liabilities) are derived by projecting forward benefit cash flows, for up to 70 years or so, and discounting these to the valuation date with an allowance for anticipated investment returns that is believed to be prudent. This is different from 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.
4. The results of the valuation have revealed a deterioration in the funding position from a shortfall of £311,000 in 2014 to a shortfall of £3,547,000 in 2017. It has been agreed by the Conference that the shortfall should be eliminated by contributions to be paid from the Pension Reserve Fund to the Scheme as follows:
  - £650,000 will be paid to the Scheme each August, starting August 2018 up to and including August 2022; and
  - Between £0 and £447,000 will be paid to the Scheme each December, starting December 2018 up to and including December 2022. The precise amount payable will be determined by the Scheme Actuary each year having regard to Scheme experience.
5. These contributions are reflected in the Recovery Plan which has been agreed and signed by the Methodist Council and the other participating employers.
6. Part of the £650,000 core contribution covers the additional shortfall arising after the valuation date as a result of the employers paying less than the required future service contribution rate over the period from 1 September 2017 to 31 August 2019 (see paragraph 9).
7. There was a significant increase in the total (employer plus member) future service contribution rate from 31.7% of pensionable earnings in 2014 to 42.6% of pensionable earnings in 2017. This increase in the future service contribution rate is mainly due to the fall in bond yields.
8. The required employer future service contribution rate would increase from 23.7% to 34.6% of pensionable earnings if the member contribution rate was maintained at the current rate of 8% of pensionable earnings and the Scheme continued in its current form.
9. The current contribution rate being paid by the employers is 24.1% of pensionable earnings. It has been agreed that the employers will continue paying 24.1% of pensionable earnings until 31 August 2019. As noted above, the additional shortfall arising over the two years until 31 August 2019 in relation to the future service underpayment has been included within the contributions to be paid in accordance with the Recovery Plan.

### The employer covenant

10. As part of the consideration of the valuation results, the Trustee must have regard to the strength of the covenant of the participating employers. The strength of the covenant helps determine how prudent the actuarial assumptions need to be.
11. As reported to the Council in April 2018, the Trustee engaged an external consultant, PwC, to conduct an external assessment of the employers' covenants to the Scheme.
12. After consideration of the PwC report and after receiving additional comfort from the Conference regarding the use of the Pension Reserve Fund, the Trustee assessed the overall covenant to the Scheme as 'tending to strong' for the purposes of the 2017 valuation.

### Prudent assumptions

13. Funding assumptions need to be made about the likely course of events.
14. 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.
15. In particular, the Pensions Regulator expects prudent assumptions to be used for the discount rate assumptions and mortality assumptions to be based on prudent principles.

### Assumptions

16. The valuation results have been produced using a set of actuarial assumptions which the Trustee Board has agreed with the FSC and the other participating employers. These assumptions are summarised below and are provided in more detail in the Statement of Funding Principles (which has been agreed and signed by the Trustee and the Connexional Treasurer on behalf of all the participating employers):

Assumption	Agreed basis for 2017 valuation	Changes from 2014 valuation basis
<b>Non-pensioner Discount Rate</b>	Bank of England gilt curve plus 2.0% pa for 3 years linearly reducing over the following 22 years to 0.5% pa in 25 years' time	Updated to reflect current market conditions, current investment strategy and updated covenant assessment, and to use term dependent assumptions.
<b>Pensioner Discount Rate</b>	Bank of England gilt curve plus 0.5% pa throughout	
<b>RPI inflation</b>	Equal to the Bank of England RPI inflation curve	Updated to reflect current market conditions and to use term-dependent assumptions
<b>CPI inflation</b>	0.75% below the Bank of England RPI inflation curve	Updated to reflect current expectations for the future
<b>Pensionable Earnings Increases</b>	Equal to CPI assumption plus an age-related promotional scale, with allowance for some members' salaries to remain frozen for three years from the valuation date	1% addition to CPI assumed at 2014 valuation removed to reflect employers' current expectations of future salary increases
<b>Pension Increases</b>	As guaranteed in the Rules, based on RPI increases, with some pensions receiving fixed 5% increases	Updated to reflect current market conditions
<b>Commutation</b>	An allowance for members to commute 10% of their pensions for a lump sum	Reduced from 15% allowance at 2014 valuation to reflect the latest Scheme experience

Assumption	Agreed basis for 2017 valuation	Changes from 2014 valuation basis
<b>Mortality</b>	Most up to date tables and improvement factors available at the valuation date	Updated to use the most up to date tables and improvement factors
<b>Expenses</b>	4.0% pa	An increase from 3.7% pa to reflect Scheme experience

### Assets

17. The assets of the Scheme (excluding the value of the insurance policies held by Legal and General) had a market value of £68,198,045 as at 31 August 2017. On the valuation basis the Scheme was 95.1% funded as at 1 September 2017.

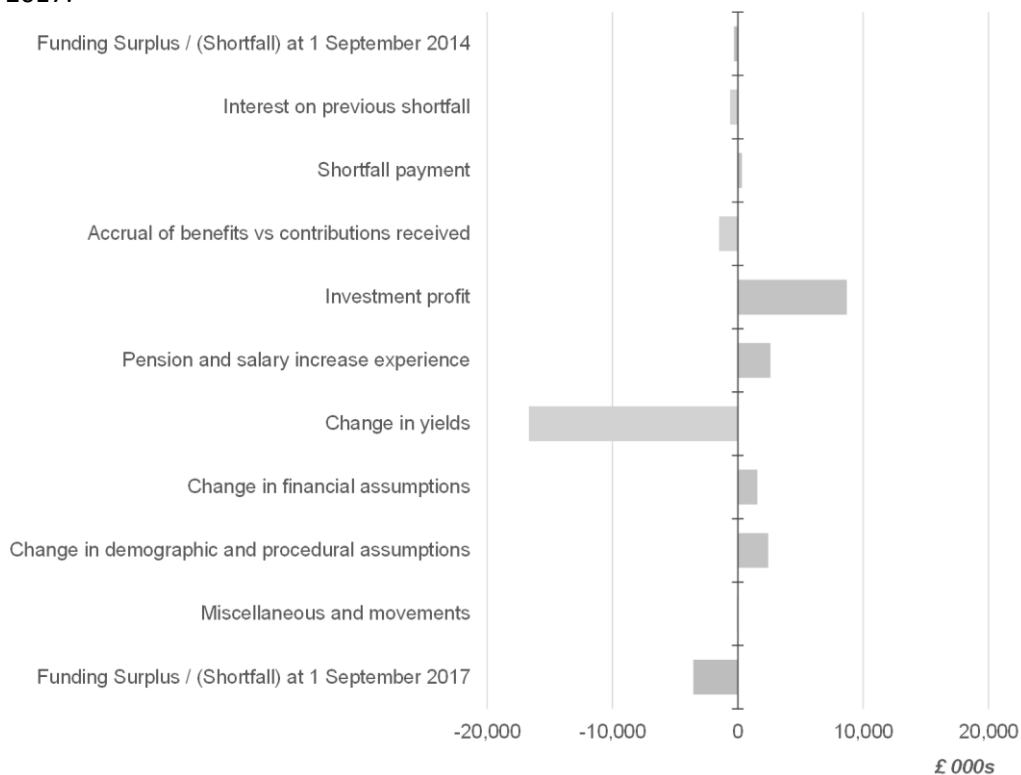
### Results

18. The table below sets out the results of the actuarial valuation as at 1 September 2017 together with the 2014 results for comparison purposes:

	2017	2014
Technical provisions (liabilities) (£'000)	71,745	51,393
Market value of assets (£'000)	68,198	51,082
Past service surplus/(shortfall) (£'000)	(3,547)	(311)
Funding ratio	95.1%	99.4%
Total future service contribution rate (% pensionable earnings)	42.6%	31.7%

### Change in funding position

19. The valuation carried out as at 1 September 2014 revealed a shortfall of £311,000. The position has deteriorated as there was a shortfall of £3,547,000 as at 1 September 2017. The graph below shows the main factors contributing to the change in funding position over the three years to 1 September 2017:



20. The graph shows that the deterioration in the funding position is primarily due to the fall in gilt yields over the inter-valuation period which places a higher value on the liabilities of the Scheme. However, this was offset to some extent by investment profit and favourable experience items.

### Membership

21. The membership profile for the 2017 valuation is shown in the table below, together with the figures for the 2014 valuation for comparison purposes.

	22 September 2017*	1 September 2014
Active	244	197
Deferred	261	247
Pensioners	212	173
Total	717	617

*\*The 2017 valuation allowed for known membership movements between 1 September 2017 and 22 September 2017.*

### Recovery plan

22. The results of the valuation revealed a deterioration in the funding position from a shortfall of £311,000 in 2014 to a shortfall of £3,547,000 in 2017. It has been agreed by the Conference that the shortfall should be eliminated by contributions to be paid from the Pension Reserve Fund to the Scheme as follows:
- £650,000 will be paid to the Scheme each August, starting August 2018 up to and including August 2022; and
  - Between £0 and £447,000 will be paid to the Scheme each December, starting December 2018 up to and including December 2022. The precise amount payable will be determined by the Scheme Actuary each year having regard to Scheme experience.
23. These contributions are reflected in the Recovery Plan which has been agreed and signed by the Methodist Council and the other participating employers.
24. Part of the £650,000 core contribution covers the additional shortfall arising after the valuation date as a result of the employers paying less than the required future service contribution rate over the period from 1 September 2017 to 31 August 2019 (see paragraph 27).

### Contributions

25. The required employer future service contribution rate would increase from 23.7% to 34.6% of pensionable earnings if the member contribution rate was maintained at the current rate of 8% of pensionable earnings and the Scheme continued in its current form.
26. The current rate being paid by the employers is 24.1% of pensionable earnings. It has been agreed that the employers will continue paying 24.1% of pensionable earnings until 31 August 2019. As noted above, the additional shortfall arising over the two years until 31 August 2019 in relation to the future service underpayment has been included within the contributions to be paid in accordance with the Recovery Plan.

### Solvency position

27. The Scheme Actuary also reviewed the position if the Scheme had been 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.
28. The solvency estimate provides an indication of the extent to which the Trustee is reliant on the employers to stand behind the Scheme.

29. The solvency position as at 1 September 2017 is set out below, together with the position at 1 September 2014:

	<b>1 September 2017</b>	<b>1 September 2014</b>
Shortfall (£'000)	30,574	18,031
Funding level	69.0%	73.9%

#### **Next steps**

30. The valuation has been finalised and no further action is required from the Methodist Council at this stage. For information, signed copies of the following documents are attached to this paper:
- Statement of Funding Principles
  - Recovery Plan
  - Schedule of Contributions
  - Formal Valuation Report (including Actuary's certification of technical provisions)
  - Certification of schedule of contributions
31. It is anticipated that the Methodist Council will be asked to consider the SRC's proposals for the future of PASLEMC at the January Council meeting.

#### **Consultation with Scheme members**

32. A consultation with members regarding the future of the Scheme is currently underway. Should the benefit structure remain unchanged, the employers would need to pay contributions of 34.6% of pensionable earnings from 1 September 2019 in order to provide the future service benefits. This is an increase of 10.5% from the current rate of contributions paid by the employers of 24.1% of pensionable earnings.
33. The consultation with members ends on 15 October and the FSC will consider the results during November and intends to present proposals to the SRC on 29 November. A proposed course of action is expected to be presented to the January Council meeting for consideration.
34. The Trustee of the Scheme will be informed of the outcome of the consultation at the appropriate time, and will take legal advice on its role in relation to it.

#### **Trivial Commutations and Small Lump Sums**

35. On a request from the Pension Scheme Trustee Board, the PASLEMC lawyers have reviewed the Scheme Rules in order to clarify the position in respect of paying lump sums in accordance with trivial commutation and de minimus lump sum legislation.
36. A Deed of Amendment was signed on 25 September 2018 which authorised the Trustee to pay members trivial commutation lump sum payments up to £10,000 in accordance with legislation as qualified in the Finance Act.

#### **\*\*\*RESOLUTIONS**

- 75/1. The Council receives the report and notes the final results of the 2017 actuarial valuation.**
- 75/2. The Council notes the update on the consultation with Scheme members regarding future benefits within the Pensions and Assurance Scheme for Lay Employees of the Methodist Church and the anticipated timetable for consideration of the responses.**
- 75/3. The Council notes the rule change in respect of de minimus payments up to £10,000.**
- 75/4. The Council notes that the Deed of Amendment clarifies the position by making reference to payments prescribed by regulation.**