Northern Ireland Local Government Officers' Superannuation Committee

Funding Strategy Statement

Last Reviewed: March 2019

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1. OVERVIEW

1.1 This Funding Strategy Statement has been prepared in accordance with Regulation 64 of the Local Government Pension Scheme Regulations (Northern Ireland) 2014 ("the Regulations"). The Statement describes the funding strategy of the Northern Ireland Local Government Officers' Superannuation Committee (NILGOSC), in its capacity as Administering Authority to the Northern Ireland Local Government Officers' Pension Fund (the Fund).

1.2 As required by regulation 64(4)(a) of the Regulations, the Statement has regard to guidance published by CIPFA.

2. PURPOSES OF THE STATEMENT

2.1 Funding is defined as the making of advance provision to meet the cost of accruing benefit promises. Decisions taken regarding the approach to funding will therefore determine the rate or pace at which this advance provision is made. Although the Regulations specify the fundamental principles on which funding contributions should be assessed, implementation of the funding strategy is the responsibility of NILGOSC, acting on the professional advice provided by the Actuary.

2.2 The purpose of this statement is to document the processes by which NILGOSC:

- establishes a clear and transparent fund-specific strategy which will establish how employers' pension liabilities are best met going forward;
- supports the desirability of maintaining as nearly constant a common contribution rate as possible;
- ensures that the regulatory requirements to set contributions to ensure that the solvency and long-term cost efficiency of the fund are met; and
- takes a prudent longer-term view of funding those liabilities.

noting that whilst the funding strategy applicable to individual employers or categories of employer must be reflected in the Funding Strategy Statement, its focus should at all times be on those actions which are in the best long-term interests of the Fund.

2.3 The intention is for this strategy to be both cohesive and comprehensive for the Fund as a whole, recognising that there will be conflicting objectives that need to be balanced and reconciled.

2.4 This Funding Strategy Statement is not an exhaustive list of policy on all issues.

3. CONSULTATION

3.1 In accordance with Regulation 64(1), all employers participating within the Fund were consulted on the contents of this Statement and their views were taken into account in formulating the final Statement. The Statement describes a single strategy for the Fund as a whole.

3.2 In addition, NILGOSC has had regard to the Fund's Statement of Investment Principles published under Regulation 10 of the Local Government Pension Scheme (Management and Investment of Funds) Regulations (Northern Ireland) 2000 (as amended) ("the Investment Regulations").

3.3 The Fund Actuary, Aon Hewitt Ltd, was also consulted on the contents of this Statement.

4. PURPOSE AND AIMS OF THE FUND

4.1 Purpose of the Fund

4.1.1 The purpose of the Fund is to maintain financial assets required for the payment of benefits as laid down in the Regulations. The Fund:-

- receives monies in respect of contributions from employers and employees, transfer values and investment income; and

- pays out monies in respect of scheme benefits, refunds, transfer values and the costs of pension administration and investment management.

4.2 AIMS OF THE FUND

4.2.1 The aims of the Fund in relation to the Funding Strategy are:-

i. **Stability** - to enable employers' contributions to be kept as nearly constant as possible and (subject to NILGOSC not taking undue risks) at reasonable cost to the Scheme Employers, Admission Bodies, other bodies and to the taxpayers while achieving and maintaining Fund solvency and long term cost efficiency, which should be assessed in light of the risk profile of the Fund and employers, and the risk appetite of NILGOSC and employers alike.

ii. **Sufficiency** - to ensure that sufficient resources will be available to meet all liabilities as they fall due.

iii. **Effectiveness -** to manage the employers' liabilities effectively.

iv. **Income Maximisation** - to maximise the income from investments within reasonable risk parameters.

4.3 THE AIMS IN PRACTICE

4.3.1 **Stability** - NILGOSC recognises that the requirement to keep employers' contributions as nearly constant as possible can run counter to the following requirements:

- the regulatory requirements to secure solvency and ensure long-term cost efficiency,
- the requirement that the costs should be reasonable, and
- maximising income from investments within reasonable risk parameters

4.3.2 Producing low volatility in employers' contributions requires material investment in assets that 'match' the employers' liabilities. In this context, 'match' means investing in very secure assets that behave in a similar manner to the liabilities as economic conditions alter. For the liabilities represented by benefits payable by the Fund, such assets would tend to comprise long-dated index-linked gilt investments. However, investing in such a matched strategy would increase employer contributions from their current levels.

4.3.3 Other classes of assets, such as shares and property, are perceived to offer higher long-term rates of return on average and, consistent with the requirement to maximise the returns from investments within reasonable risk parameters, NILGOSC invests a substantial proportion of the Fund in such assets. However, these assets attract more risk by nature, and that risk can manifest itself in volatile returns over short-term periods and a failure to deliver the expected return in the long term.

4.3.4 This short-term volatility in investment returns can produce a consequent volatility in the measured funding position of the Fund at successive valuations, with knock-on effects on employers' contributions.

4.3.5 **Sufficiency** - NILGOSC recognises the need to ensure that the Fund has, at all times, sufficient liquid assets to be able to pay pensions, refunds, transfer values, costs, charges and other expenses. It is NILGOSC's policy that such expenditure is met, in the first instance, from incoming employers' and employees' contributions to avoid the expense of disinvesting assets. NILGOSC monitors the position on a daily basis to ensure that all cash requirements can be met.

4.3.6 **Effectiveness** - NILGOSC seeks to ensure that all employers' liabilities are managed effectively. In a funding context, this is achieved by seeking regular actuarial advice, ensuring that employers are properly informed through regular monitoring of the funding position, appropriate segregation of employers for funding purposes and the outlook for employers' contributions after the next triennial actuarial valuation.

4.3.7 **Income Maximisation** - NILGOSC recognises the desirability of maximising investment income within reasonable risk parameters through investment in unmatched investments. Investment returns higher than those available on holding index-linked gilts are sought through investment in other asset classes such as shares and property. NILGOSC ensures that risk parameters are reasonable by:

- Restricting investment to the levels permitted by the Investment Regulations;
- limiting default risk by restricting investment to asset classes generally recognised as appropriate for UK pension funds;
- analysing the volatility and absolute return risks represented by those asset classes in collaboration with the Fund's Actuary, Investment Advisors and Fund Investment Managers and ensuring that they remain consistent with the risk and return profiles anticipated in the funding strategy;
- limiting concentration risk by developing a diversified asset strategy; and
- monitoring the mis-matching risk that the investments do not move in line with the Fund's liabilities.

5. RESPONSIBILITIES OF THE KEY PARTIES

5.1 Although a number of parties, including bankers, custodians, investment fund managers, legal and investment advisers and external auditors, have responsibilities to the Fund, the key parties for the strategy are seen as NILGOSC, each individual employer and the Fund Actuary.

5.2 RESPONSIBILITIES OF NILGOSC

5.2.1 NILGOSC should administer the pension fund.

5.2.2 NILGOSC should collect investment income and other amounts due to the Fund as stipulated in the Regulations including employers' and employees' contributions and, as far as NILGOSC is able to, ensure these contributions are paid by the due date. Details of how it meets this requirement are shown below:-

- Individual employers must pay contributions in accordance with regulations 73, 74 and 75 of the Regulations. NILGOSC has advised all employers of its policy on the remittance of pension contributions and the procedures which will apply in the event of late or non-payment, including the requirement to report material breaches of the law to the Pensions Regulator.
- Employers' contributions are due to NILGOSC on the first day of the month following the month that they were deducted from employees' pay. If contributions are overdue by 10 days NILGOSC will levy an interest charge in accordance with Regulation 77(4).
- NILGOSC will ensure that action is taken to recover liabilities from employing authorities (including admission bodies) that cease to participate in the Fund. The Fund Actuary will calculate the exit payment due at the date of exit of the employer and NILGOSC will notify the employer of the exit payment required to meet any

deficit at the exit of the employer.

5.2.3 NILGOSC should pay from the Fund the relevant entitlements as stipulated by the Regulations.

5.2.4 NILGOSC should invest surplus monies in accordance with the Investment Regulations. It does this by ensuring that NILGOSC's Statement of Investment Principles complies with the Investment Regulations.

5.2.5 NILGOSC should ensure that cash is available to meet liabilities as and when they fall due. NILGOSC monitors the position on a daily basis to ensure that all cash requirements can be met.

5.2.6 NILGOSC should manage the valuation process in consultation with the Fund Actuary. NILGOSC ensures it communicates effectively with the Fund Actuary to:

- agree timescales for the provision of information and provision of triennial valuation results;
- ensure provision of data of suitable accuracy;
- ensure that the Fund Actuary is clear about the Funding Strategy, including the setting of grouped or individually assessed employer contribution rates under Regulation 68(7);
- ensure that participating employers receive appropriate communication throughout the process; and
- ensure that reports are made available as required by Guidance and Regulation.

5.2.7 NILGOSC shall take measures to safeguard the Fund against the consequences of employer default.

5.2.8 The application of individually assessed employer contributions includes but is not limited to the following types of employers:

- those admission bodies that have closed to new entrants;
- those employers that have joined the Fund in recent years;
- any admission bodies (e.g. contractors) that join for a limited period;
- those employers who are funding one-off strain costs through employers' contributions; and
- those employers which are assessed by NILGOSC as having a weak covenant. NILGOSC will carry out an employer covenant assessment exercise on a triennial basis to assess the strength of covenant of each of the employers in the fund and will regularly monitor covenant strength between triennial assessments.

5.2.9 NILGOSC is required to prepare and maintain a Statement of Investment Principles and a Funding Strategy Statement after due consultation with interested parties. NILGOSC will comply with the Regulations and follow Best Practice in the formulation of both of these policies.

5.2.10 NILGOSC will monitor all aspects of the Fund's performance and funding and amend the Statement of Investment Principles or Funding Strategy Statement if required. NILGOSC monitors the funding position and the investment performance of the Fund on a quarterly basis.

5.2.11 NILGOSC will effectively manage any potential conflicts of interest arising from its dual role as both Administering Authority and Scheme Employer.

5.3 RESPONSIBILITIES OF INDIVIDUAL EMPLOYERS

5.3.1 Individual employers are responsible for:

- complying with the Regulations;
- deducting contributions from employees' pay;
- paying all ongoing contributions, including their employers' contribution as determined by the Actuary, promptly by the due date;
- developing a policy on certain discretions and exercising discretions within the regulatory framework and ensuring NILGOSC has copies of current policies covering those discretions;
- paying additional contributions in accordance with agreed arrangements;
- paying the capital costs resulting from early retirements, augmentation of membership, additional pension, exercises of discretion allowing the early payment of deferred benefits or any other one-off strain costs. Payment is due immediately;
- notifying NILGOSC promptly of all changes to membership, or other changes, which affect future funding;
- providing the information requested by NILGOSC for employer covenant assessment exercises on a timely basis;
- paying any exit payments on ceasing to participate in the Fund; and
- noting and, if desired, responding to consultations regarding the Funding Strategy Statement.

5.4 RESPONSIBILITIES OF THE FUND ACTUARY

5.4.1 The Actuary will prepare advice and calculations and provide advice on

- Funding strategy and the preparation of the Funding Strategy Statement and will prepare valuations and issue a Rates and Adjustments Certificate. This includes the setting of employers' contribution rates at a level to ensure fund solvency and long-term cost efficiency, after agreeing assumptions with NILGOSC and having regard to the Funding Strategy Statement and relevant admission agreements. Valuations will be carried out and reported on in accordance with the Technical Actuarial Standards as issued by the Financial Reporting Council as appropriate;

- Bulk transfers;
- Individual benefit related matters such as pension strain costs, ill-health retirement costs, compensatory added years costs, etc;
- Valuations on the cessation of admission agreements or when a body ceases to employ any active members;
- Bonds and other forms of security to NILGOSC against the financial effect on the Fund of employers' default; and
- Such advice will take account of the funding position and Funding Strategy Statement, along with other relevant matters when instructed to do so.

5.4.2 The Actuary will assist NILGOSC in assessing whether employer contributions need to be revised between valuations as permitted or required by the Regulations.

5.4.3 The Actuary will ensure that NILGOSC is aware of any professional guidance or other professional requirements which may be of relevance to his or her role in advising the Fund.

6. SOLVENCY TARGET AND FUNDING TARGET

6.1 NILGOSC will prudently seek to secure the solvency of the Fund over the long term. For this purpose NILGOSC defines solvency as being achieved when the value of the Fund's assets is greater than or equal to the value of the Fund's liabilities in respect of service prior to the measurement date. NILGOSC believes that its funding strategy will ensure the solvency of the Fund because employers collectively have the financial capacity to increase employer contributions should future circumstances require, in order to continue to target a funding level of 100%.

6.2 For all grouped employers (see below), and other employers of strong covenant whose participation is indefinite in nature or which have a commitment from such an employer to subsume the assets and liabilities post-exit, the Solvency Target is based on a prudent assumption that the Fund's investments will deliver long-term returns above pension increases and revaluation of pension accounts (CPI) after the Trajectory Period (defined in Section 7.4).

6.3 The Funding Target for the grouped employers is not necessarily the same as the Solvency Target and is, instead the product of the data, chosen assumptions and valuation method. The key component is the discount rate, which, for the grouped employers allows for the long-term investment strategy of the Fund and NILGOSC's chosen probability of funding success, i.e. the chosen chance of achieving the Solvency Target at the end of the Trajectory Period.

6.4 For ungrouped employers whose participation in the Fund is believed to be of limited duration through known constraints or through reduced covenant, and for which no access to further funding would be available to the Fund after exit, (i.e. the liabilities would become orphan) the solvency target will be set at a level higher than that for grouped employers, dependent on circumstances. NILGOSC will have regard to the potential for participation to cease (or for the body to have no contributing members), the potential timing of such exit, and any likely change in notional or actual investment strategy as regards the assets held in respect of the body's liabilities at the date of exit (i.e. whether the liabilities will become 'orphaned' or a guarantor exists to subsume the notional assets and liabilities).

6.5 Where the liabilities will become orphaned the funding target will assume investment in an appropriate portfolio of government index linked and fixed interest bonds after exit. This is known as the ongoing orphan funding target. Allowance may be made for expected increases in gilt yields after the valuation date and for expected outperformance of the Fund's assets in the period before exit so this is not the same as the exit basis, which for orphan liabilities makes no allowance for any outperformance of the Fund's assets over and above the redemption yield on long-dated gilts.

6.6 For employing authorities which are removed from the Main group but where it is possible that they might be re-admitted to the Group (e.g. on securing a guarantee and commitment from a Government Department to fund the liabilities should the employer exit), NILGOSC may assume continued investment in a broad range of assets of higher risk than risk free assets for a longer period, albeit it will still consider any likely change in notional or actual investment strategy as regards the assets held in respect of the body's liabilities when the employer exits. This is known as the intermediate funding target.

7. FUNDING STRATEGY

7.1 Risk based approach

7.1.1 The Fund utilises a risk-based approach to funding strategy.

A risk-based approach entails carrying out the valuation on the basis of the assessed likelihood of meeting the funding objectives, rather than relying on a 'deterministic' approach which gives little idea of the associated risk. In practice, three key decisions are required for the risk-based approach -

- what the Solvency Target should be (your funding objective - where you want to get to),
- the Trajectory Period (how quickly you want to get there), and
- the Probability of Funding Success (how likely you want it to be now that you will actually achieve the Solvency Target by the end of the Trajectory Period).

These three choices, supported by complex risk modelling carried out by the Actuary, define the discount rate (investment return assumption) to be adopted and, by extension, employer contributions payable. Together they measure the riskiness of the funding strategy.

7.2 GROUPING

7.2.1 For the purposes of setting minimum employer contribution rates at triennial Fund valuations, certain employers are grouped together and contributions are set based on all employers in the group sharing all funding risks. Employers which are grouped should note that the consequent smoothed contribution rate payable may be higher or lower than the rate that would otherwise be payable if grouping did not exist and the rate was set by reference to the Employers' own membership characteristics and underlying asset share.

7.2.2 Between the 2004 and 2019 valuations, the grouping only applied in respect of setting employer rates at triennial valuations. Each employer was notionally allocated a notional asset share of the Fund at the 2004 Fund valuation, or at subsequent commencement in the Fund and these notional asset shares were tracked since that date. From the 1 April 2019 valuation all risks and experience will be pooled (shared) for employers in the group. At each future triennial valuation, the notional asset share will only be tracked across the group allowing for investment returns, cashflows and expenses attributable to the group etc. For the purpose of employer accounting or other calculations where a notional asset figure is required for an employer within the group, all grouped employers will be allocated a notional share of the group assets in the same proportion to their liabilities, i.e. they are all assumed to have the same funding level.

7.2.3 Further detail of how the grouping arrangements are allowed for in employer calculations will be available from the Actuary via NILGOSC.

7.2.4 Employers can elect to pay contributions above the minimum level set by NILGOSC but in the case of employers within the Main group such contributions will be allocated to the Main group as a whole rather than to the employer making the payment. In order to ensure that other employers in the Main group do not have to pay for the decisions of individual employers within the Main group, key elements of experience will be monitored and employers asked to make additional contributions to cover the assessed cost of any additional liabilities arising due to decisions they have made.

7.2.5 All employers in the Fund are grouped with the exception of employers which are known to be closed to new entrants or employers which display characteristics that are not in line with the Main group, including those employers assessed by NILGOSC as having a weak covenant as part of an employer covenant assessment.

7.2.6 Death-in-service and ill-health benefits are shared (pooled) across all employers in the Fund regardless of whether or not they participate in the Main group.

7.2.7 Where Employers are required to produce annual accounting figures under Financial Reporting Standard 102 (FRS102) or International Accounting Standard 19 (IAS19) and these are produced by the Fund Actuary, these will use the employer's notional asset share from the latest valuation (or accounting position if later) as their starting point (see 7.2.3 above) and the requirements of the relevant accounting standards. Employers should note that because the accounting and the funding calculations are used for different purposes and are subject to different regulatory and other requirements, they may be very different. Furthermore, unless specifically requested, any FRS102/IAS19 accounting figures supplied by the Fund Actuary for an Employer will not make any allowance for the potential use of more prudent assumptions in an exit valuation, unless specifically requested.

7.3 ACHIEVING SOLVENCY THROUGH PAYMENT OF SMOOTH EMPLOYER CONTRIBUTION RATES

7.3.1 Consistent with the aim of enabling employers' contribution rates to be kept as nearly constant as possible:

- Contribution rates are set by use of the Projected Unit valuation method for most employers. The Projected Unit method is used in the actuarial valuation to determine the cost of benefits accruing to the Fund for employers who continue to admit new members. This means that the contribution rate is derived as the cost of benefits accruing to employee members over the year following the valuation date expressed as a percentage of members' pensionable pay over that period;

- The Attained Age method is normally used for employers who no longer admit new members. This means that the contribution rate is derived as the average cost of benefits accruing to members over the period until they die, leave the Fund or retire; and

- The required chance of achieving solvency at the end of the relevant Trajectory Period for each employer or employer group can be altered at successive valuations within an overall envelope of acceptable risk.

7.3.2 NILGOSC will not permit contributions to be set following a valuation that have an unacceptably low chance of achieving the Solvency Target at the end of the relevant Trajectory Period. Similarly, the rate will not be set at a level that gives rise to additional costs for example, where deferring costs to the future would be likely to result in those costs being greater overall than if they were provided for at the time.

7.4 RECOVERY PERIOD AND TRAJECTORY PERIOD

7.4.1 The Trajectory Period is the period between the valuation date and the date on which solvency is targeted to be achieved. For employers in the Main group this is set to be an appropriate long-term period over which NILGOSC wish to achieve the solvency target.

7.4.2 Where a valuation reveals that the Fund is in surplus or deficiency against the Funding Target, employers' contributions will be adjusted to target restoration of the solvent position over a period of years (the Recovery Period). The Recovery Period is therefore a period over which any adjustment to the level of contributions in respect of any surplus or deficiency relative to the Funding Target used in the valuation is payable. As noted above, the valuation method, including the components of Funding Target, future service costs and any adjustment for surplus or deficiency simply serve to set a level of contributions payable, which in turn dictates the chance of achieving the Solvency Target at the end of the Trajectory Period.

7.4.3 NILGOSC recognises that a large proportion of the Fund's liabilities are expected to give rise to benefit payments over long periods of time. NILGOSC recognises the risk in relying on long recovery periods and has agreed with the Fund Actuary a limit of 20 years for the Recovery Periods for those employers assessed by NILGOSC as having a strong covenant whose participation is indefinite in nature, principally those in the Main group.

Recovery Periods for employers outside of the group may be shorter than those employers in paragraph 7.4.3, in order to suitably balance risk to the Fund and cost to the employer. The Recovery Period applicable for each ungrouped employer is set by NILGOSC in consultation with the Fund Actuary, with a view to balancing the various funding requirements against the risks involved due to such issues as the financial strength of the employer and the nature of its participation in the Fund e.g. the future working lifetime will be used for employers which are closed to new entrants in the majority of cases.

7.5 TREATMENT AND RECOVERY OF DEFICITS WHEN AN EMPLOYER LEAVES THE FUND

7.5.1 When an organisation participating in the Fund ceases to have any active members, NILGOSC will decide whether the employer is to be treated as having withdrawn from the Fund and an exit valuation is therefore to be carried out immediately, or whether the exit valuation can be deferred under provision of Regulation 70(12) of the Regulations.

7.5.2 Where the employer is deemed to have withdrawn from the Fund, the Fund Actuary will carry out an exit valuation to determine any exit payment due from or surplus due to the outgoing organisation. NILGOSC will recover any exit payment from that organisation unless there is a successor organisation under an apportionment agreement, which is also a participating employer in the Fund, which formally adopts the pension liabilities of the previous organisation as its own. Any surplus due will be paid to the outgoing organisation.

7.5.3 Where an exit payment is recoverable from an outgoing organisation, that exit payment will generally be required to be paid immediately. However, NILGOSC does have discretion to agree more flexible terms provided that such terms do not place the Fund at material risk.

7.5.4 The purpose of an exit valuation is to remove as much of the risk as possible of remaining Fund employers being asked to make contributions in future to meet the liabilities of departed employers. In light of this, the financial and demographic assumptions adopted by the Fund Actuary in respect of an exit valuation may be different (more prudent) than those adopted for an ongoing valuation as described elsewhere in this statement.

7.5.5 In determining the assumptions to be adopted the Fund Actuary will consider whether the liabilities will become orphan (i.e. no ongoing employer will be responsible for funding the liabilities) or whether the assets and liabilities will be transferred to ("subsumed by") a long-term secure employer in the Fund. In the case of the former, makes no allowance for any outperformance of the Fund's assets over and above the redemption yield on long-dated gilts.

7.5.6 NILGOSC will take the following into account in determining whether or not an exit valuation can be deferred under Regulation 70(12):

- The financial position of the employer on deferral;
- The employer's funding position at the date of deferral;
- The future working lifetime of the active members immediately before the date of exit;

- The Funding Strategy Statement and funding target applicable to the employer during the deferral period;
- Specifics of the legal agreement with the Employer;
- Any actuarial or legal advice; and
- Any individual circumstances relevant to the request for deferral of the exit valuation

Further detail is set out in the Committee's Admission and Exit Policy

7.5.7 NILGOSC has a policy of requiring admission bodies to obtain a guarantor. A guarantor is required to agree that it will meet the shortfall if the admission body closes and cannot pay the contributions due.

7.5.8 If an employer (other than an admission body falling within paragraph 2(1)(h)(i) of Part 1 of Schedule 2 of the Regulations) fails and the contributions due cannot be met by the employer, its guarantor or any bond, the Regulations require that all employers in the Fund must pay revised contributions to meet the shortfall.

7.5.9 If an admission body falling within paragraph 2(1)(h)(i) of Part 1 of Schedule 2 of the Regulations fails and it and/or any bond provider cannot meet some or all of the contributions due, the regulations require that the related employer in relation to that admission body or guarantor must pay revised contributions to meet the balance.

7.5.10 Liabilities in the Fund in respect of former employing authorities which are already orphaned will be assumed to be 100% funded on the appropriate funding target at each valuation. This will be achieved by notionally re-allocating assets within the Fund as required.

7.6 EMPLOYER CONTRIBUTION RATES

7.6.1 Employer contributions will be expressed as two separate elements:

(i) a percentage of pensionable pay in respect of future accrual of benefits (future funding rate).

(ii) where a funding deficit is identified, defined streams of capital contributions in respect of deficit recovery (rather than a percentage of payroll), increasing annually as determined by NILGOSC in consultation with the Fund Actuary.

7.6.2 Where the Employer or Main group is in surplus, NILGOSC will consider, in consultation with the Fund Actuary:

- whether Employer contributions for the Main group or any ungrouped employer may be reduced below that required to meet the cost of future accrual of benefits for that employer or Main group to allow that surplus to be run off over a suitable period; and
- how any existing stream of capital contributions certified for employers in the Main group is adjusted or reduced in light of the surplus which has arisen.

7.6.3 In determining the approach to be adopted where the valuation discloses a surplus of assets relative to the funding target, NILGOSC's overriding aim will to be to ensure any reduction in employer contributions is not deemed to lead to an unacceptable risk of contributions needing to be increased again in future, bearing in mind the overriding aim of the funding strategy is to keep contributions stable.

7.6.4 Consistent with the requirement to keep employer contributions as nearly constant as possible, NILGOSC will consider, at each valuation, whether new contributions should be payable immediately, or should be reached by a series of steps over future years. NILGOSC will discuss with the Fund Actuary the risks inherent in such an approach and will examine the financial impact and risks associated with each employer.

7.6.5 NILGOSC adopts a contribution strategy that limits changes to the future service rate to plus or minus 1% of pay per annum for all employers in the Main group. NILGOSC will review this strategy every three years in conjunction with the actuarial valuation. This policy does not apply to those Employers who do not fall into this category and a contribution rate will be based on their own experience using methods and assumptions consistent with the Fund's funding and investment strategies and suitably balancing risk to the Fund and cost to the Employer.

7.6.6 Where defined streams of capital contributions are required for deficit recovery, NILGOSC will review at future valuations whether any new emerging surplus or deficiency will give rise to a new, separate defined stream of contributions, or will be consolidated with any existing stream of contributions into one new defined stream of contributions. In particular, NILGOSC will determine how any emerging surplus or deficiency within the Main group will be apportioned between the employers in the group, with a view to adopting an approach which balances the need to act equitably between employers in the group and to adopt a cost effective, practical approach.

7.7 LONG-TERM COST EFFICIENCY

7.7.1 In order to ensure that measures taken to maintain stability of employer contributions are not inconsistent with the statutory objective for employer contributions to be set so as to ensure the long-term cost efficiency of the Fund, NILGOSC has assessed the actual contributions payable by considering:

- The implied average deficit recovery period, allowing for the stepping of employer contribution changes;
- The investment return required to achieve full funding over the recovery period; and
- How the investment return compares to NILGOSC's view of the expected future return being targeted by the Fund’s investment strategy.

7.8 TRACKING OF ASSET SHARES BETWEEN TRIENNIAL VALUATIONS

7.8.1 For employers in the Main group, the notional asset share for the whole group will be tracked allowing for all cashflows associated with the membership of the entire group, including contribution income, benefit outgo, transfers in and out and investment income allocated as set out below. In general, no allowance is made for the timing of contributions and cashflows for each year are assumed to be made halfway through the year with investment returns assumed to be uniformly earned over that year. Further adjustments are made for:

- A notional deduction to meet the expenses paid from the Fund in line with the assumption used at the previous valuation;
- Allowance for any known material internal transfers in the Fund (cashflows will not exist for these transfers) where these involve employers outside of the Group. Appendix 1 and the Admission and Exit Policy set out how these will be calculated, noting that in general the Fund Actuary will distinguish between individual transfers and TUPE transfers;
- Allowance for lump sum and dependants' pensions following death in service, ill health retirements, and any other benefits shared across all employers; and
- An overall adjustment to ensure the total notional assets attributed to each employer is equal to the total assets of the Fund, which will take into account any gains or losses related to the orphan liabilities.

7.8.2 Individual employers in the group will be allocated the same proportion of notional assets as all other employers in the group, relative to the calculated level of their liabilities.

7.8.3 For employers outside of the Main group, the notional asset share allocated to each employer will normally be calculated using the same approach as described in 7.8.1 above allowing for historic cashflows of the individual employer.

7.9 ATTRIBUTION OF INVESTMENT INCOME

7.9.1 NILGOSC has a single investment strategy and the Main group's and ungrouped employers' notional asset shares will generally be credited with the rate of return earned by the Fund assets as a whole, adjusted for any return credited to those ungrouped employers for whom a tailored notional investment portfolio exists.

7.9.2 Where NILGOSC has determined that it is appropriate for an employer to have a tailored investment portfolio notionally allocated to it, the notional asset share for that employer will be credited with a rate of return appropriate to the agreed notional investment portfolio.

7.10 MONITORING OF THE FUNDING LEVEL BETWEEN VALUATIONS

7.10.1 NILGOSC will monitor the funding position between triennial valuations, generally at a whole of Fund level. If it is considered appropriate, an indicative interim valuation will be carried out. The purpose of this monitoring process is to give employers advance warning of likely changes that may be required following the next triennial valuation. This allows improved budgeting decisions to be made and allows an employer outside of the Main group to take an informed decision on paying contributions over and above the minimum required.

7.11 BULK TRANSFERS AND APPORTIONMENTS

7.11.1 Bulk transfers of staff can occur between two employers which participate in the Fund (an internal transfer), or between an employer in the Fund and an employer not in the Fund (an external transfer).

7.11.2 In such circumstances NILGOSC will be mindful of the potential impact of the transfer on any employers in the Fund and, where either employer is in the Fund and grouped for funding purposes, the group as a whole. Therefore, whilst in the first instance the level of transfer can be a matter for agreement by the employer or employers affected, NILGOSC can and must retain a degree of interest and control in the process.

7.11.3 NILGOSC's Bulk Transfer Policy is attached at Appendix 1.

7.12 BONDS AND OTHER SECURITISATION

7.12.1 Paragraph 1 of Part 2 of Schedule 2 of the Regulations creates a requirement for

- in the case of a body admitted under paragraph 2(1)(h)(i) of Part 1 of Schedule 2 of the Regulations, the employing authority; or
- in all other cases, the admission body, to the satisfaction of NILGOSC,

to carry out an assessment taking account of actuarial advice, of the level of risk arising on premature termination of the provision of service or assets by reason of insolvency, winding up or liquidation of the admission body.

7.12.2 Where the level of risk identified by the assessment is such as to require it, the admission body shall enter into an indemnity or bond with an appropriate party. Where, for any reason it is not possible for an admission body to enter into an indemnity bond, the admission body is required to secure a guarantee in a form satisfactory to NILGOSC from an organisation who either funds, owns or controls the functions of that admission body.

7.12.3 NILGOSC's approach in this area is as follows:

- In the case of Admission Bodies admitted under paragraph 2(1)(h)(i) of Part 1 of Schedule 2 of the Regulations and other Admission Bodies with a Guarantor, and so long as NILGOSC judges the relevant Scheme Employer or guarantor to be of sufficiently sound covenant, any bond exists purely to protect the relevant Scheme Employer or Guarantor on default of the admission body. As such, the relevant Scheme Employer or Guarantor must arrange a risk assessment and decide the level of required bond (if any) from the Admission Body, if any.
- In the case of -
  i. Admission Bodies admitted under paragraph 2(1)(h)(ii) of Part 1 of Schedule 2 of the Regulations,
  ii. Admission Bodies admitted under paragraph 2(1)(h)(i) of Part

1 of Schedule 2 of the Regulations where NILGOSC judges the employer not to be of sound covenant, and

iii. any other Admission Bodies where there is no guarantor or NILGOSC judges the guarantor not to be of sound covenant,

the admission will only be able to proceed once NILGOSC has agreed the level of bond cover. As such, NILGOSC will obtain some "standard" calculations from the Fund Actuary to assist them to form a view on what level of bond would be satisfactory. NILGOSC, on request, will supply this calculation to the employer or guarantor, where relevant, but this should not be construed as advice to the employer or guarantor on this matter.

7.12.4 NILGOSC notes that levels of required bond cover can fluctuate and will review or recommend that the employer reviews, the required cover regularly, at least once a year.

8. IDENTIFICATION OF RISKS AND COUNTER MEASURES

8.1 NILGOSC's overall policy on risk is to identify all risks to the Fund and to consider the position both in aggregate and at an individual risk level. NILGOSC will monitor the risks to the Fund, and will take appropriate action to limit the impact of these both before, and after, they emerge wherever possible. The main risks to the Fund are captured in the following tables:

Risk	Explanation
Liability Risk	This covers items such as demographic risks, pay and price inflation varying from anticipated levels, or the effect of possible increases in employer contribution rates on service delivery and on employers. The main demographic risks include changing retirement patterns, ill health and longevity. NILGOSC will ensure that the Fund Actuary investigates these matters at each valuation or, if appropriate, more frequently, and reports on developments. NILGOSC will agree with the Fund Actuary any changes that are necessary to the assumptions underlying the measure of solvency to allow for observed or anticipated changes. If significant changes become apparent between valuations, NILGOSC will notify all participating employers of the anticipated impact on costs that will emerge at the next valuation and will review any guarantees that are in place for any admission bodies that have been admitted to the Fund.

Risk	Explanation
Investment risk	This covers items such as the performance of financial markets and the Fund's investment managers, asset reallocation in volatile markets, leading to the risk of investments not performing (income) or increasing in value (growth) as forecast. Examples of specific risks would be: • assets not delivering the required return (for whatever reason, including manager underperformance) • systemic risk with the possibility of interlinked and simultaneous financial market volatility • insufficient funds to meet liabilities as they fall due • inadequate, inappropriate or incomplete investment and actuarial advice is taken and acted upon • counterparty failure The specific risks associated with assets and asset classes are: equities – industry, country, size and stock risks • index-linked gilts – interest rate risk, inflation risk • return seeking bonds – credit risk, interest rate risk, derivative risk including counterparty risk, liquidity risk, manager risk • alternative assets – liquidity risks, property risk, alpha risk • money market – credit risk and liquidity risk • currency risk • macroeconomic risks NILGOSC reviews each investment manager's performance quarterly and considers the asset allocation of the Fund formally by carrying out a triennial review with its Investment Advisors, Fund Managers and Fund Actuary.

Risk	Explanation
Employer Risk	These risks arise from the ever-changing mix of employers; from short-term and ceasing employers; and the potential for a shortfall in payments and/or orphaned liabilities. NILGOSC will put in place a Funding Strategy Statement which contains sufficient detail on how funding risks are managed in respect of the main categories of employer (e.g. scheduled and admission bodies) and other pension fund stakeholders. NILGOSC maintains a knowledge base on their admission bodies and their legal status (charities, companies limited by guarantee, group/subsidiary arrangements) and uses this information to inform the Funding Strategy Statement. NILGOSC carries out a covenant assessment exercise at least every three years to assess the strength of covenant of each of the employers in the fund and uses this information to inform the valuation. NILGOSC pools the risk associated with death-in-service and ill-health early retirement across all employers in the Fund. This reduces the risk of the funding position of a small, ungrouped employer being materially affected by a death-in-service or ill-health early retirement.
Regulatory and Compliance Risk	The risks relate to changes to both general and LGPS specific regulations, national pension requirements or HM Revenue and Customs' rules. NILGOSC will keep abreast of all proposed changes to the LGPS. If any change potentially affects the costs of the Fund, NILGOSC will ask the Fund Actuary to assess the possible impact on costs of the change. Where significant, NILGOSC will notify employers of the possible impact and the timing of any change.

Liquidity and maturity risk	The LGPS is going through a series of changes, each of which will impact upon the maturity profile of the LGPS and have potential cash flow implications. The increased emphasis on outsourcing and other alternative models for service delivery may result in the following: • active members leaving the LGPS, • transfer of responsibility between different public sector bodies, • scheme changes which might lead to increased opt-outs • spending cuts and their implications All of these may result in workforce reductions that would reduce membership, reduce contributions and prematurely increase retirements in ways that may not have been taken into account in previous forecasts. NILGOSC's policy is to require regular communication between itself and employers and to ensure reviews of maturity at overall Fund and employer level where material issues are identified.

Risk	Explanation
Governance	This covers the risk of unexpected structural changes in the Fund membership (for example the closure of an employer to new entrants or the large-scale withdrawal or retirement of groups of staff) and the related risk of NILGOSC not being made aware of such changes in a timely manner. NILGOSC's policy is to require regular communication between itself and employers and to ensure regular reviews of such items as guaranteed bond arrangements and funding levels. NILGOSC seeks to ensure that each employer complies with its Admission Agreement (if applicable) and the Scheme Regulations.
Solvency measure	NILGOSC recognises that allowing for future investment returns in excess of those available on government bonds introduces an element of risk, in that those additional returns may not materialise. NILGOSC's policy will be to monitor the probability of the returns required to achieve solvency to ensure that the funding strategy remains acceptable relative to the agreed risk envelope.
Recovery period	NILGOSC recognises that permitting the Solvency Target to be achieved over a period rather than immediately introduces a risk that action to restore solvency is insufficient between successive measurements. NILGOSC's policy is to discuss the risks inherent in each situation with the Fund Actuary and to limit the permitted length of recovery period to no longer than 20 years. For closed employers the Recovery Period will only be permitted to exceed the future working lifetime of the active members as calculated by the Fund Actuary in exceptional circumstances. This limits the exposure of the Fund to potential adverse consequences which can arise due to increasing volatility of contribution requirements for the closed employer as membership declines.

Risk	Explanation
Grouped Contribution Risk	NILGOSC recognises that grouping the majority of employers for the purpose of setting the minimum contribution rate(s) introduces a risk that the contributions paid by certain employers in the group will not target their individual prospective liabilities. NILGOSC's policy is • to discuss the risks inherent in each situation with the Fund Actuary, to understand the nature and level of the risk • to remove employers which close to new members or display characteristics that are not in line with the group from the grouped contribution rate • to monitor experience of employers in the Group in relation to risks under an employer's control (e.g. pay growth) to ensure that other employers in the Group are not unfairly paying for additional liabilities created by the behaviour/choices of certain employers in the Group • to communicate the risk of underpaying or overpaying contributions to employers in the group.
Default	NILGOSC is alert to the possibility that an Employer may default on any exit payment or other debt owed to the fund and will seek to ensure that the pace of funding for Employers will reasonably balance consequent costs against the exposure borne by the Fund or any guarantors. NILGOSC will also ensure that guarantees are in place where the Regulations allow or will seek legal redress to ensure the fund does not suffer a loss.

9. LINKS TO INVESTMENT POLICY AS SET OUT IN THE STATEMENT OF INVESTMENT PRINCIPLES

9.1 NILGOSC has produced this Funding Strategy Statement having taken an overall view of the level of risk in the investment policy set out in the Statement of Investment Principles and the funding policy set out in this statement.

9.2 The current strategic asset allocation is based upon a triennial review carried out by NILGOSC and the resulting Asset Allocation is set out in NILGOSC's Statement of Investment Principles, which was last updated on 27 February 2018.

9.3 NILGOSC will continue to monitor the suitability of the investment policy overall, and in respect of individual employers in the light of the Fund's developing liabilities, funding strategy and finances.

9.4 NILGOSC will continue to review the Funding Strategy Statement and the Statement of Investment Principles to ensure that the overall risk profile remains appropriate. Such reviews may use asset liability modelling or other analysis techniques.

10. FUTURE MONITORING

10.1 NILGOSC plans to review formally this Statement as part of each triennial valuation process unless circumstances arise which require earlier action.

10.2 NILGOSC will monitor the funding position of the Fund on an approximate basis at regular intervals between valuations and will discuss with the Fund Actuary whether any significant changes have arisen that require action.

APPENDIX 1

BULK TRANSFER POLICY

Background

A bulk transfer may arise when two or more members are transferred between employers, for example on a re-organisation of public services.

This Bulk Transfer policy applies to all employers participating in the Fund. This policy summarises how NILGOSC manages bulk transfers, the approaches that will usually be adopted to determine the amount of the bulk transfer and when additional funding or other payments may be required. The circumstances relevant to any particular case will be considered.

Bulk transfers from the Fund are specifically governed by regulations 110 and 111 of the Local Government Pension Scheme Regulations (Northern Ireland) 2014. Nothing within this policy can take precedent over the relevant legislation.

ASSET SHARES

As a general principle, and subject to other overriding factors, NILGOSC and the Fund Actuary will use the asset shares attributable to the transferring employer at the date of transfer in setting the level of transfer (rather than the Fund as a whole). The asset share in relation to employers in the Main group will be determined as set out earlier in this statement.

Additionally, unless the ceding employer will become an exiting employer, assets assumed to be held to meet the transferring liabilities will generally be calculated in proportion to the assets notionally held to cover the remaining liabilities of the transferring employer (i.e. the employer which employed the transferring members before the transfer date) with no adjustment to ensure that non-active liabilities of the transferring employer remain fully funded.

Where the employer is grouped with other employers (see section 7.2), the assets are not notionally apportioned to employers within the group at each valuation because this is not needed for the purpose of setting employer contributions. Where asset values are required, e.g. for employer accounting or exit valuations, the asset share will be calculated assuming all grouped employers have the same funding level relative to their liabilities.

In bulk transfer cases the asset share for an employer in the group will be determined by applying the estimated group funding ratio at the transfer date to the value of the transferring liabilities, where the group liabilities are assessed based on assumptions consistent with those used for the group at the last triennial valuation of the Fund updated for changes in market conditions and any change in the funding strategy statement as appropriate.

INTERNAL BULK TRANSFERS WITHIN THE FUND

These will arise when there is a bulk transfer of members from an existing Scheme employer to another Scheme employer e.g. as part of government re-organisation or an outsourcing. It is usual for those members who are transferred to have continuous membership in the Scheme, unless they opt out. This means that their full service built up to the date of the transfer would transfer to the new employer.

In general, the Fund's approach is to require additional funding where needed to reduce the risk to the Fund. However, this will depend upon the circumstances and the employers involved in the transfer:

The Fund's approach to grouping means that in general, there is no need to calculate a notional asset transfer where there is an internal transfer from one grouped employer to another grouped employer between valuations. Any deficit contributions payable by the transferring and receiving employers will not change as a result of internal transfers unless any surplus or deficit in relation to the transferring liabilities is being passed from the ceding employer to the receiving employer and this is deemed to be sufficiently material to warrant amending their contributions. The total contributions payable by grouped employers should not change by virtue of the transfer of liabilities between employers in the group.

If it is a transfer to a newly admitted Scheme employer e.g. due to an outsourcing, the new employer will usually commence fully funded with a funding target appropriate to that employer. Where the transfer is from an ungrouped employer the transferring employer will be required to make an immediate payment in respect of any funding shortfall attributable to the members who are transferring to the new employer. Where the transfer is from an employer within the Main group, where the surplus or deficit on the transferring liabilities is being retained within the Main group and the ceding employer's contributions have been set to allow for any surplus or deficit the transferring employer's contributions do not need to be amended.

Whenever liabilities are transferred to an inheriting body such as a Scheme employer using an apportionment agreement[1] and the inheriting body accepts future responsibility for funding the full liabilities, including any shortfall there will be no need to require any additional contributions by virtue of the transfer.

Other internal transfers, where the liabilities transferring are material to either the transferring or receiving employer, will be executed by reference to similar principles modified if appropriate due to the circumstances of the transfer in question and any relevant external factors. In particular:

- Where several staff transfer from one employer in the Main group to another in the Main group, the grouping mechanism means that no formal calculations are required, and the assets notionally allocated to each employer will be rebalanced in line with the movement in liabilities at the following triennial valuation.

- Where members are transferring from an employer in the Main group to an employer not in the Main group, the liabilities which have transferred will typically be valued on a more prudent funding target for the ungrouped employer than if they remained in the Main group. In that case, the assets which will be transferred will be considered on a case-by-case basis with the aim of ensuring a fair and proportionate approach for the circumstances and employers concerned.

[1] The Local Government Pension Scheme Regulations (Northern Ireland) 2014, regulation 71

- Where members are transferring from an employer outside of the Main group to an employer in the Main group, the reverse is true, i.e. the liabilities which have transferred will typically be valued on a less prudent funding target for the Main group employer than if they remained with the ungrouped employer. In that case, the assets which will be transferred will be considered on a case-by-case basis with the aim of ensuring a fair and proportionate approach for the circumstances and employers concerned.

- Where members are transferring in bulk from an existing employer in the Main group to new employer which is to be outside of the Main group (and the transfer is on the date of commencement), the liabilities which transfer will typically be calculated on a more prudent funding target for the new ungrouped employer than if they remained in the Main employer group. In most cases, e.g. if the transfer is due to an outsourcing, the assets which will be transferred will be such that the employer commences without a funding deficit in relation to those transferring members. This may require a contribution from the ceding employer in order to make good any funding shortfall.

INTERNAL TRANSFERS (WHERE NOT IN BULK)

Members may also transfer within the Fund on an individual basis where TUPE does not apply e.g. by moving to a new job with a different employer. If the member elects to aggregate their previous benefits accrued with their old employer with their new benefits, then responsibility for their accrued benefits will transfer to their new employer.

Where the transfer is between employers in the Main group the assets in the group are not notionally allocated between the employers for the purpose of setting contributions at each actuarial valuation (and where assets shares are required for employer accounting or other purposes they will be apportioned pro rata to the employer’s share of the group’s liabilities on the funding basis). Where both employers are in the Main group there is therefore no need to explicitly calculate an asset transfer in respect of the transferring liabilities and there is an implicit assumption that the transfer will be on a share of fund basis.

Where the transfer involves an employer who is outside of the Main group, it is necessary to consider what level of assets should notionally transfer between the employers in respect of these liabilities. In general, NILGOSC's approach is for the transferring assets to be calculated on a cash equivalent transfer value (CETV) basis (i.e. as if the members were taking individual transfers).

However, where members are transferring from an employer in the Main employer group to one of the employers not in the Main group, the liabilities which transfer will typically be calculated on a more prudent funding target for the ungrouped employer than if they remained in the Main employer group. This means that the assets which transfer are likely to be lower in value than the liabilities, resulting in an immediate deficit in respect of those members for the receiving employer.

Whilst the individual cash equivalent approach is the default, NILGOSC will consider such cases on an individual basis, depending upon the nature of the transfers and their materiality to the employers. The principles which NILGOSC will apply are to ensure fairness between employers with an overriding objective of protecting the Fund. Where a transfer of assets above the level of a CETV is transferred from the

Main Group to an ungrouped employer in relation to an individual transfer of liabilities, the Main Group employer may, at NILGOSC's discretion and on actuarial advice, be asked to make an additional payment to ensure there is no reduction in the group's overall funding level.

EXTERNAL BULK TRANSFERS OUT TO AN EMPLOYER OUTSIDE THE FUND

Generally, NILGOSC will offer a 'capped share of fund' transfer, such that any funding shortfall in respect of the transferring members would be transferred to the receiving employer but no surplus would be transferred. Any shortfall is usually dealt with outside the Fund e.g. by a top up payment from the employer to the receiving scheme. In the event of a funding surplus the bulk transfer value will be capped at the value of the transferring members' liabilities calculated on the funding target appropriate to the paying employer.

Some exceptions to this are:

- Where the transferring employer has exited, or is expected to shortly exit the Fund, a 'reserved share of fund', will normally be used. This means that NILGOSC will firstly reserve in full for any non-transferring liabilities that it will retain, for example those liabilities relating to deferred members, pensioners and any non-transferring active members. This would generally be calculated on a low risk basis.

- Where the transferring employer makes immediate payment of any shortfall attributable to the transferring members or arising from the transfer, enabling a fully funded transfer to be paid.

- Any other circumstances which may be agreed between NILGOSC and the Fund Actuary and notified in writing to the transferring employer.

BULK TRANSFERS INTO THE FUND

There is no provision to allow for bulk transfers into the Fund and any incoming bulk transfer value will be dealt with in the same way as individual transfers.