
EARLY RETIREMENT STRAIN FACTORS

Report by Service Director HR and Communications

JOINT MEETING OF PENSION FUND COMMITTEE AND PENSION BOARD

16 September 2021

1 PURPOSE AND SUMMARY

- 1.1 This report advises on a review that has been undertaken by Hymans Robertson of the Early Retirement Strain Cost Factors for Scottish Borders Council Pension Fund and proposes the implementation of the amended factors, along with a commitment to review these as part of the triennial valuation going forward. The manual that has been provided as part of the review will remain current and ensure that these are interpreted and applied in the correct manner now and in the future.**
- 1.2 The Fund needs strain cost factors to determine the added cash which an employer must pay whenever a member takes early retirement on unreduced benefits. These benefits cost the Fund more than it had been expecting, so the employer must pay the additional cost.
- 1.3 The current Fund factors, which have not been reviewed since 2005, have been compared to the proposed factors, the current factors overstate the strain cost in most circumstances, and therefore adopting the new factors will generally give rise to lower strain costs required from employers. The proposed factors are outlined within **Appendix 1**.
- 1.4 The Pensions Administration Team will look to implement the new factors in accordance with the best practice advice provided by Hymans Robertson, which is outlined at section 4.5 of the report.

2 RECOMMENDATIONS

- 2.1 It is recommended that the Pension Fund Committee:**
 - (a) Approves the implementation of the new Early Retirement Strain Cost Factors;**
 - (b) Approves the review of Early Retirement Strain Cost Factors at each future triennial valuation;**
 - (c) Notes the provision of the Manual for future reference.**

3 BACKGROUND

3.1 At the triennial valuation, the Fund Actuary calculates the estimated cost of providing benefits to members, over and above the member contributions and expected investment returns. This estimated cost is then charged to employers as their required regular contributions. In valuing the benefits, the Actuary generally assumes that active members will start taking benefits around the earliest date they are able to do so in full, the "Normal Pension Age" or NPA.

LGPS Regulations determine the NPA for different tranches of benefit for a given member, and the employer contributions are based on that data. If a member was to take early retirement on unreduced benefits before NPA then an added cost arises for the Fund. This is due to:

- The longer expected payment period: the member's expected age at death is unchanged, but the start date of payments is earlier;
- The missing investment returns which the Fund would have expected on those assets if they hadn't been needed for early retirement benefit payments, but had remained invested until NPA instead (this is partly offset by the expected future salary and CPI growth which would have increased the benefits).

3.2 The early retirement strain factors have been based on the provisions of the Local Government Pension Scheme (Scotland) Regulations 2018 as they apply as of July 2021 and refer to awards in the following circumstances:-

- Unreduced benefits on grounds of redundancy or business efficiency (Regulation 29(8)).
- Unreduced benefits where a reduction is waived with employer consent or Administering Authority consent (where the original employer is no longer a Scheme employer) between ages 55 and 60 (Regulation 29(6) & (9)).
- Unreduced, and in some cases reduced benefits, on flexible retirement (Regulation 29(7)).

3.3 Regulation 63(2) of the Local Government Pension Scheme (Scotland) Regulations 2018 provides the power to the Administering Authority to require employers to make additional payment(s) to the Fund, as determined by the Fund actuary, to cover a strain arising from the early payment of pension benefits. Hymans Robertson, the Fund Actuary, have confirmed the method of calculation of the strain and in particular the basis for the proposed new factors.

3.4 The cost of any award of additional pension awarded under Regulations 16 or 30 of the Local Government Pension Scheme (Scotland) Regulations 2018 should be calculated separately and is payable to the Fund in addition to the amount of any early retirement strain determined in accordance with this report. Determination of the costs of purchasing or awarding additional pension is carried out in accordance with regulations 16 or 30 and is covered by appropriate guidance issued by the Government Actuary's Department (GAD).

4 EARLY RETIREMENT STRAIN FACTOR REVIEW

- 4.1 Hymans Robertson have been commissioned to carry out the review of the factors and their report is attached at **Appendix 1**.
- 4.2 Hymans Robertson have carried the review out using the same set of assumptions as those used to underpin the most recent funding valuation. The Pensions Administration software only allows for one set of table factors to be applied, therefore a pragmatic approach has been taken and the assumptions as applied to the majority of the Fund members have been used in this review: -
- Assumed investment return = 3.8% p.a.
 - Pay growth rate = 2.6% p.a.
 - Pension increase rate = 1.9% p.a.
 - Life expectancy as per whole Fund averages.
- Due to only one factor being permitted within the Administration software the average of the Female and Male factors have been taken.
- 4.3 The above assumptions are also in line with the assumptions underpinning the majority of employer funding strategies as at the last valuation. If different assumptions were to be adopted for these factors, then there would be a disconnect between the measurement of the required strain payment, and the measurement of the existing funding reserve immediately prior to early retirement.
- 4.4 Officers did not ask Hymans to consider a more or less prudent set of assumptions as it is important that the connection to the valuation assumptions is maintained and these can then be used in future reviews.
- 4.5 In order to assist with the implementation and interpretation of the Early Strain Factors the provision of an Instruction Manual has also been commissioned by Officers. This will ensure the correct and timely application of the new factors, following the guidance at pages 9/10 of Appendix 1, along with the additional material included in the Instruction Manual now and in the future when reviews are carried out.
- 4.6 The proposed factors give a decrease in strain costs, at an average of 5%, when compared to the existing factors. This can be attributed to: -
- (a) a likely lower post-retirement assumed real investment return above CPI pension increases and an increased likely assumed longevity assumption (both giving rise to higher annuity factors)
 - (b) being more than offset by;
 - (c) a likely lower pre-retirement assumed real investment return above pay growth (which gives a lower ERR factor) alongside the removal of the 25% loading
- 4.7 The following table show the current and proposed factors: -

Years to Funded Retirement Date	Existing Factors	Proposed Factors
0 (or past FRD already)	0.00%	0.00%
1	4.50%	4.17%
2	8.80%	8.03%
3	12.90%	11.63%
4	16.82%	14.96%
5	20.56%	18.05%
6	24.14%	20.93%
7	27.55%	23.61%
8	30.81%	25.57%
9	33.93%	27.38%
10	36.90%	29.08%
11	39.74%	30.68%
12	42.45%	32.21%
13	45.04%	33.66%
14	47.51%	35.04%
15	49.88%	36.37%

5 IMPLICATIONS

5.1 Financial

The cost of carrying out the review of the Early Retirement Factors is £2,950.00 plus VAT and for the production of the supporting Manual £3,250.00 plus VAT.

There are no further financial implications for the Fund and the proposed new factors will ensure the Fund is appropriately compensated for any early retirements.

5.2 Risk and Mitigations

By undertaking this review and then building this in as a standard review as part of the triennial valuation ensures that the factors used in early retirement situations are current and based on the latest assumptions, this mitigates against the risk of the factors becoming outdated and the Fund either receiving too little or too much when early retirements are granted.

5.3 Integrated Impact Assessment

There is no impact or relevance to Equality Duty or the Fairer Scotland Duty for this report. This is routine good governance required under the Local Government Pension Scheme (Governance) (Scotland) Regulations 2014. Nevertheless, a light touch assessment has been conducted and this will be published on SBC's Equality and Diversity Pages of the website demonstrates that equality, diversity and socio-economic factors have duly been considered when preparing this report.

5.4 Sustainable Development Goals

There are no direct economic, social or environmental issues with this report which could affect the Council's sustainability.

5.5 Climate Change

There are no direct climate change impacts as a result of this report.

5.6 Rural Proofing

This report does not relate to new or amended policy or strategy and as a result rural proofing is not an applicable consideration.

5.7 Data Protection Impact Statement

There are no personal data implications arising from the proposals contained in this report.

5.8 Changes to Scheme of Administration or Scheme of Delegation

No changes to either the Scheme of Administration or the Scheme of Delegation are required as a result of this report.

6 CONSULTATION

- 6.1 The Executive Director (Finance & Regulatory), the Monitoring Officer/Chief Legal Officer, the Chief Officer Audit and Risk, the Clerk to the Council and Corporate Communications have been consulted and any comments received have been incorporated into the final report.

Approved by

Clair Hepburn

Service Director HR and Communications

Signature

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Background Papers:

Previous Minute Reference: 24 September 2020

Note – You can get this document on tape, in Braille, large print and various computer formats by contacting the address below. Ian Angus can also give information on other language translations as well as providing additional copies.

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