

Royal Borough of Kensington and Chelsea Pension Fund

IAS26 Disclosures as at 31 March 2012

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Public Sector Consulting

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1. Introduction

We have been instructed by Royal Borough of Kensington and Chelsea, the Administering Authority to the Royal Borough of Kensington and Chelsea Pension Fund (“the Fund”), to provide pension disclosures in respect of pension benefits provided by the Local Government Pension Scheme (“the LGPS”) to members of Royal Borough of Kensington and Chelsea Pension Fund (“the Fund”) as at 31 March 2012.

This report is addressed to the Administering Authority and its advisers; in particular, this report is likely to be of relevance to the Fund’s auditor.

These figures have been prepared in accordance with IAS26. In calculating the disclosed numbers we have adopted methods and assumptions that are consistent with IAS19.

This advice complies with all Generic Technical Actuarial Standards (TASs) and the Pensions TAS.

The LGPS is a defined benefit statutory scheme administered in accordance with the Local Government Pension Scheme Regulations 2007/08, as amended. It is contracted out of the State Second Pension.

2. Valuation Data

Data Sources

In completing our calculations for IAS26 purposes we have used the following items of data, which we received from Royal Borough of Kensington and Chelsea:

- The results of the Triennial Actuarial Valuation as at 31 March 2010 which was carried out for funding purposes;
- Estimated whole fund income and expenditure items for the period to 31 March 2012;
- Estimated whole fund returns for the period to 31 March 2012 based on assets used for the purpose of the IAS26 valuation as at 31 March 2011, actual fund returns for the period to 31 March 2012 and then market returns (estimated where necessary) for the balance of the period (if necessary) to 31 March 2012;
- Details of any new early retirements for the period to 31 March 2012 that have been paid out on an unreduced basis, which are not anticipated in the normal employer service cost.

Although some of these data items have been estimated, we do not believe that they are likely to have a material effect on the results of this report, especially in the context of the roll-forward approach we have taken (as described in the next section). Further, we are not aware of any material changes or events since we received the data.

Employer Membership Statistics

The table below summarises the membership data as at 31 March 2010.

| Member Data Summary | Number | Salaries/Pensions £000's | Average Age |
|---------------------|--------|-----------------------------|-------------|
| Actives | 3,416 | 97,043 | 44 |
| Deferred Pensioners | 3,296 | 7,393 | 45 |
| Pensioners | 2,220 | 14,529 | 70 |

Assets

The return on the Fund (on a bid value to bid value basis) for the year to 31 March 2012 is estimated to be 5%. This is based on the estimated Fund value used at the previous accounting date and the estimated Fund value used at this accounting date. The actual return on Fund assets over the year may be different.

The estimated asset allocation for Royal Borough of Kensington and Chelsea Pension Fund as at 31 March 2012 is as follows:

| Employer Asset Share - Bid Value | 31 March 2012 | | 31 March 2011 | |
|----------------------------------|----------------|-------------|----------------|-------------|
| | £000's | % | £000's | % |
| Equities | 347,267 | 64% | 427,742 | 83% |
| Gilts | 5,426 | 1% | 51,535 | 10% |
| Other Bonds | 0 | 0% | 0 | 0% |
| Property | 21,704 | 4% | 20,614 | 4% |
| Cash | 5,426 | 1% | 15,461 | 3% |
| Alternative Assets | 162,781 | 30% | 0 | 0% |
| Total | 542,604 | 100% | 515,352 | 100% |

The final asset allocation of the Fund assets as at 31 March 2012 may be different from that shown due to estimation techniques.

3. Actuarial Methods and Assumptions

Roll-Forward Approach

To assess the value of the Employer's liabilities as at 31 March 2012, we have rolled forward the value of the Employer's liabilities calculated for the Triennial valuation as 31 March 2010 allowing for the different financial assumptions required under IAS19.

The full actuarial valuation involved projecting future cashflows to be paid from the Fund and placing a value on them. These cashflows include pensions currently being paid to members of the Scheme as well as pensions (and lump sums) that may be payable in future to members of the Fund or their dependants. These pensions are linked to inflation and will normally be payable on retirement for the life of the member or a dependant following a member's death.

It is not possible to assess the accuracy of the estimated liability as at 31 March 2012 without completing a full valuation. However we are satisfied that the approach of rolling forward the previous valuation results to 31 March 2012 should not introduce any material distortions in the results provided that the actual experience of the Employer and the Fund has been broadly in line with the underlying assumptions, and that the structure of the liabilities is substantially the same as at the latest formal valuation. From the information we have received there appears no evidence that this approach is inappropriate.

Demographic/Statistical Assumptions

We have adopted a set of demographic assumptions that are consistent with those used for the formal funding valuation as at 31 March 2010. The post retirement mortality is based on S1PA Heavy tables allowing for medium cohort projection, with a minimum 1% improvement for future life expectancies.

The assumed life expectations from age 65 are:

| Life Expectancy from age 65 (years) | 31 March 2012 | 31 March 2011 |
|-------------------------------------|---------------|---------------|
| Retiring Today | | |
| Males | 19.0 | 18.9 |
| Females | 23.1 | 23.0 |
| Retiring in 20 years | | |
| Males | 21.0 | 20.9 |
| Females | 25.0 | 24.9 |

We have also made the following assumptions:

- Members will exchange half of their commutable pension for cash at retirement
- Active members will retire one year later than they are first able to do so without reduction

Financial Assumptions

The financial assumptions used for the purposes of the calculations are as follows.

| Assumptions as at | 31 March 2012 | | 31 March 2011 | | 31 March 2010 | |
|-------------------|---------------|-------|---------------|-------|---------------|------|
| | % p.a. | Real | % p.a. | Real | % p.a. | Real |
| RPI Increases | 3.3% | - | 3.5% | - | 3.9% | - |
| CPI increases | 2.5% | -0.8% | 2.7% | -0.8% | n/a | |
| Salary Increases | 4.7% | 1.4% | 5.0% | 1.5% | 5.4% | 1.5% |
| Pension Increases | 2.5% | -0.8% | 2.7% | -0.8% | 3.9% | - |
| Discount Rate | 4.6% | 1.3% | 5.5% | 1.9% | 5.5% | 1.5% |

These assumptions are set with reference to market conditions at 31 March 2012. The discount rate is the yield on the iBoxx AA rated over 15 year corporate bond index as at this date which has been chosen to meet the requirements of IAS19. The RPI increase assumption is set based on the difference between conventional gilt yields and index-linked gilt yields at the accounting date using data published by the Bank of England. This measure has historically overestimated future increases in the RPI and so we have made a deduction of 0.25% to get the RPI assumption of 3.3%. As future pension increases are expected to be based on CPI rather than RPI, we have made a further assumption about CPI which is that it will be 0.8% below RPI i.e. 2.5%.

Salary increases are then assumed to be 1.4% above RPI in addition to a promotional scale. This includes an adjustment to the long term assumption which we have made to allow for Government plans to set pay awards in the public sector at an average of 1% per annum for two years after the current public sector pay freeze ends.

4. Results and Disclosures

The results of our calculations for the year ended 31 March 2012 are set out in Appendix 1. We estimate that the net liability as at 31 March 2012 is a liability of £290,228,000.

In addition, Appendix 2 details a reconciliation of assets and liabilities during the year.

The figures in this report are presented only for the purposes of IAS 26. In particular, they are not relevant for calculations undertaken for funding purposes or for other statutory purposes under UK pensions legislation.

We would be pleased to answer any questions arising from this report.



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Partner**



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Appendix 1. Balance Sheet Disclosure as at 31 March 2012

| Net Pension Asset as at | 31 Mar 2012 | 31 Mar 2011 | 31 Mar 2010 |
|---|----------------|----------------|----------------|
| | £000's | £000's | £000's |
| Present Value of Funded Obligation | 832,832 | 664,742 | 751,428 |
| Fair Value of Scheme Assets (bid value) | 542,604 | 515,352 | 463,026 |
| Net Liability | 290,228 | 149,390 | 288,402 |

*Present Value of Funded Obligation consists of £658,167,000 in respect of Vested Obligation and £174,665,000 in respect of Non-Vested Obligation.

Appendix 2. Asset and Benefit Obligation Reconciliation for the Year to 31 March 2012

| Reconciliation of opening & closing balances of the present value of the defined benefit obligation | Year to 31 March 2012 £000's | Year to 31 March 2011 £000's |
|---|------------------------------------|------------------------------------|
| Opening Defined Benefit Obligation | 664,742 | 751,428 |
| Service cost | 18,212 | 24,442 |
| Interest cost | 37,441 | 41,675 |
| Actuarial losses (gains) | 113,644 | (74,669) |
| Losses (gains) on curtailments | 1,557 | 44 |
| Liabilities extinguished on settlements | - | - |
| Liabilities assumed in a business combination | 16,576 | - |
| Estimated benefits paid net of transfers in | (25,654) | (18,490) |
| Past service cost | - | (66,518) |
| Contributions by Scheme participants | 6,314 | 6,830 |
| Unfunded pension payments | - | - |
| Closing Defined Benefit Obligation | 832,832 | 664,742 |

Unfunded liabilities are normally excluded as these are liabilities of employers rather than the Pension Fund. However, all employers with unfunded pension liabilities opted to capitalise these benefits as at 31 March 2011; these new funded liabilities appear as 'Liabilities assumed in a business combination' in the table above.

| Reconciliation of opening & closing balances of the fair value of Scheme assets | Year to | Year to |
|---|----------------|----------------|
| | 31 March 2012 | 31 March 2011 |
| | £000's | £000's |
| Opening fair value of Scheme assets | 515,352 | 463,026 |
| Expected return on Scheme assets | 31,230 | 27,356 |
| Actuarial gains (losses) | (4,327) | 15,651 |
| Contributions by employer | 19,689 | 20,979 |
| Contributions by Scheme participants | 6,314 | 6,830 |
| Assets acquired in a business combination | - | - |
| Estimated benefits paid net of transfers in | (25,654) | (18,490) |
| Receipt / (Payment) of bulk transfer value | - | - |
| Fair value of Scheme assets at end of period | 542,604 | 515,352 |

| Reconciliation of opening & closing surplus | Year to | Year to |
|---|------------------|------------------|
| | 31 March 2012 | 31 March 2011 |
| | £000's | £000's |
| Surplus (Deficit) at beginning of the year | (149,390) | (288,402) |
| Current Service Cost | (18,212) | (24,442) |
| Employer Contributions | 19,689 | 20,979 |
| Unfunded pension payments | - | - |
| Past Service Costs | - | 66,518 |
| Other Finance Income | (6,211) | (14,319) |
| Settlements and Curtailments | (18,133) | (44) |
| Actuarial gains (losses) | (117,971) | 90,320 |
| Surplus (Deficit) at end of the year | (290,228) | (149,390) |