HYMANS ROBERTSON

Briefing note

IAS19/FRS102 as at 31 March 2020: Results Commentary **April 2020**

Default accounting assumptions as at 31 March 2020

Weighted average duration	Discount rate	RPI inflation (CPI)
Less than 17 years (Short)	2.3%	2.9% (2.0%)
Between 17 and 23 years (Medium)	2.3%	2.8% (1.9%)
More than 23 years (Long)	2.3%	2.7% (1.8%)

The approach to setting these default Local Government Pension Scheme accounting assumptions at 31 March 2020 is set out in full in our accompanying Accounting Assumptions Briefing Note (issued February 2020).

Results commentary

This update should be considered as an illustrative guide to the main issues affecting most employers, rather than a detailed explanation of your own experience.

For 31 March 2020, it is difficult to comment on how a 'typical' LGPS employer's balance sheet may compare to March 2019. For all LGPS Funds, investment returns have been significantly lower than expected (particularly in the last 2 months of the accounting period) which has served to worsen the balance sheet position. The effect of this will have been at least partly offset by a higher net discount rate which serves to reduce the value placed on the obligations (corporate bond yields are at a similar level to 2019 but inflation expectations are significantly lower). In addition, each employer's accounting results will reflect their own specific circumstances which could introduce differences (e.g. your LGPS cashflow position and your individual LGPS Fund's actual asset experience).

The 2019/20 charge to Profit & Loss (P&L) is based on financial conditions at the start of the year (i.e. assumptions as at 31 March 2019). The service cost and net interest cost for 2019/20 should be broadly in line with the projections made in our 2019 reports. Lastly, due to the higher net discount rate at 31 March 2020, the projected 2020/21 charge to P&L is likely to decrease compared to 2018/19.

Further, the effect of asset returns and/or financial assumption changes on the 2020 balance sheet (and the projected 2020/21 charge to Profit & Loss) may be overshadowed by the effect of the 2019 formal actuarial valuation calculations and the resulting 'step-change' in the roll forward approach. **More details on the impact of the 2019 English and Welsh formal actuarial valuations are set out in the below Appendix on page 3.**

Choice of assumptions

The accounting assumptions adopted are the responsibility of each organisation's directors (or equivalent) based on actuarial advice. Employers can take more control of the figures disclosed in their pension accounts by investigating the assumptions adopted.

We strongly recommend that, alongside your auditor, you consider the suitability of the default financial, longevity and other demographic assumptions for your specific organisation.

It is up to you to determine how to proceed with the choice of assumptions given the relative importance of the LGPS accounting figures to your organisation's own circumstances.

Further, after receiving results on the default assumptions, employers can still discuss with us their accounting figures and revisit the assumptions should this be required. This can be done by Hymans Robertson and does not require you to appoint a separate adviser for that purpose.

Contact details

For assumptions advice or for further assistance with your Results, please get in touch with our accounting specialists at:

LGPSCentralAccountingTeam@hymans.co.uk

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Appendix

Impact of the 31 March 2019 English and Welsh formal actuarial valuations

Formal actuarial valuations are carried out every three years, where each employer's assets and liabilities are calculated on a detailed basis, using individual member data, for cash contribution setting purposes. The 31 March 2019 formal valuations for English and Welsh LGPS Funds were concluded by 31 March 2020.

The accounting balance sheet position as at 31 March 2020, and the projected charge to the P&L for 2020/21, are therefore based on this new roll forward from the 2019 formal valuation. This differs to the balance sheet position as at 31 March 2019 and the charge to the P&L for 2019/20, which were based on a roll forward from the 2016 formal valuation. **This 'step change' can lead to sizeable asset and liability 'remeasurement experience' items in the reconciliation of the balance sheet from 31 March 2019 to 31 March 2020.**

For accounting purposes we project forward the results from the most recently completed formal valuation: we only allow for certain elements of experience since the formal valuation date, such as actual investment return, contributions paid, estimated benefit outgo, actual early retirements and actual outsourcings/bulk transfers when advised to do so by the employer. As such, the accuracy of the accounting projection declines over time. We would typically expect our projections to be within +/-2% of the underlying position for each year of projection. However, greater differences are possible, particularly if there have been volatile financial market movements or significant membership changes.

The asset and liability 'remeasurement experience' items arise because in the accounting roll-forward we cannot recognise all possible elements of membership experience, and these are recognised in the formal valuation calculations. **In effect, our accounting figures are "re-calibrated" every three years following each formal valuation.** For example;

- Membership movements (new entrants, withdrawals, ill health retirements, transfers etc) – any movements different to those assumed within the previous formal valuation will contribute positively or negatively to the asset and liability 'experience' items.
- Actual level of salary/pension increases – lower than expected salary growth over the previous inter-valuation period would lead to a positive liability 'experience' item (i.e. lower past service liabilities) and vice versa.
- Outsourcings / Bulk transfers – where the employer has chosen, due to materiality, not to recognise outsourcings and bulk transfers in their accounting position, the impact of these will be included in the asset and liability 'experience' items.

In line with the accounting standards, the liability 'experience' item is identified separately in the reconciliation, however the asset 'experience' item is included in the re-measurement 'return on assets' item shown in Other Comprehensive Income (OCI). In non-valuation years, the 'return on assets' item reflects the difference between actual returns over the year and the expected return (recognised in the P&L as the interest income on assets). At first glance, the 2019/20 'excess return on assets' item may appear unusual but this is likely to be due to the inclusion of any asset 'remeasurement experience' from the 2019 formal actuarial valuation 'step-change'.

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