

Staff and Pensions Committee

12 June 2023

Warwickshire Pension Fund - Revision of Early Retirement Strain Cost Factors

Recommendation

That the Committee reviews the information provided in this report and ratifies the revision of the Early Retirement Strain Cost Loading Factor for the Warwickshire Pension Fund.

1. Executive Summary

- 1.1 The Warwickshire Pension Fund has just completed its triennial valuation where the Fund's Actuary, Hymans Robertson, calculates the estimated costs to Employers of the Fund of providing benefits to members.
- 1.2 As part of the valuation the Fund has considered whether a full review of the Early Retirement Strain Cost factors should also be undertaken. These factors are used to calculate the additional cost for allowing members to retire before their normal pension age (NPA) and where their benefits are paid unreduced. The factors depend on actuarial assumptions which were reviewed and updated at the 2022 valuation.
- 1.3 There were no material changes to the actuarial assumptions as part of the 2022 valuation. Given this, and that a review of the factors was last undertaken in 2019, at the last valuation, it was decided that only a review of the loading factor be completed at this time (instead of more in-depth review).
- 1.4 The recommendation is that a new loading factor of 122% is applied to the factors that are used to derive early retirement strain costs.
- 1.5 The recommendation is also that the loading factor be implemented from 1st July 2023 and used for all future calculations to derive the strain cost payable by the employer immediately upon the member's early retirement.

2. Financial Implications

- 2.1 If a member takes early retirement with no corresponding reduction to their benefits, there are additional costs to the fund based on the longer than expected payment period and the lost investment returns. These additional costs are known as 'early retirement strain costs'.
- 2.2 As the true cost of a retirement can only be realised when the pension ceases to be paid, these strain costs are an estimate of the additional benefits that will need to be paid out of the Fund.
- 2.3 The strain cost is payable immediately upon the member's retirement. The estimated strain cost payable by the employer is calculated using factors, (unreduced pension) x (Early Retirement Reduction (ERR) Factor) x (annuity Factor at Early Retirement Age)

ERR factor = the reduction factor that would have been applied to the member's pension had they not retired with unreduced benefits

Annuity Factor = the cost of paying £1 per annum (plus future increases in payment) for the remainder of the member's lifetime from their retirement date.

- 2.4 This approach does involve some approximations, but the Fund Actuary believes these are appropriate to balance accuracy against administrative ease. Given that approximations are involved, the strain costs calculated may or may not be equal to the actual real cost of the early release of the benefits. However, any difference will be picked up in the next valuation and all additional costs will be paid to the Fund.
- 2.5 The use of these factors is a pragmatic approach to ensure the cost is collected from the member's employer at the time of the member's retirement and the additional costs are recognised by employers and fed into their decision making processes.
- 2.6 The increase in the loading factor will mean an increase in the strain costs payable by employers.

3. Environmental Implications

None arising from this report.

4. Supporting Information

- 4.1 It has been recommended by the Fund's Actuary, that the loading factor is revised immediately, as the current Early Retirement Strain Cost Factors are understating the strain cost in most circumstances.

5. Timescales associated with the decision and next steps

- 5.1 Subject to approval the change to the loading factor will be made from 1st July 2023.
- 5.2 Employers who have received a quotation of strain costs prior to this date, have been pre-emptively warned that the factors used to calculate costs are under review and so this may change the costs quoted to them.
- 5.3 However, we will review this on a case-by-case basis, looking at the date the quote was requested and the retirement date for the member, to see if a revised strain cost should be provided or whether the quotation should be honoured.

Appendices

Appendix 1 – Early Retirement Strain Cost Factors report from Hymans Robertson

Background Papers

None

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The report was circulated to the following members prior to publication:

Local Member(s):not applicable

Other members: Cllrs Dahmash and Gifford