momentum

Actuarial Valuation

of the

Cape Retirement Fund for Local Government

as at

30 June 2014

2 March 2015

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Appendices

Section 1 Executive summary

I take pleasure in presenting the results of the statutory actuarial valuation as at 30 June 2014 to the Trustees of the Cape Retirement Fund for Local Government (the Fund). The results presented in this report are based on audited financial statements.

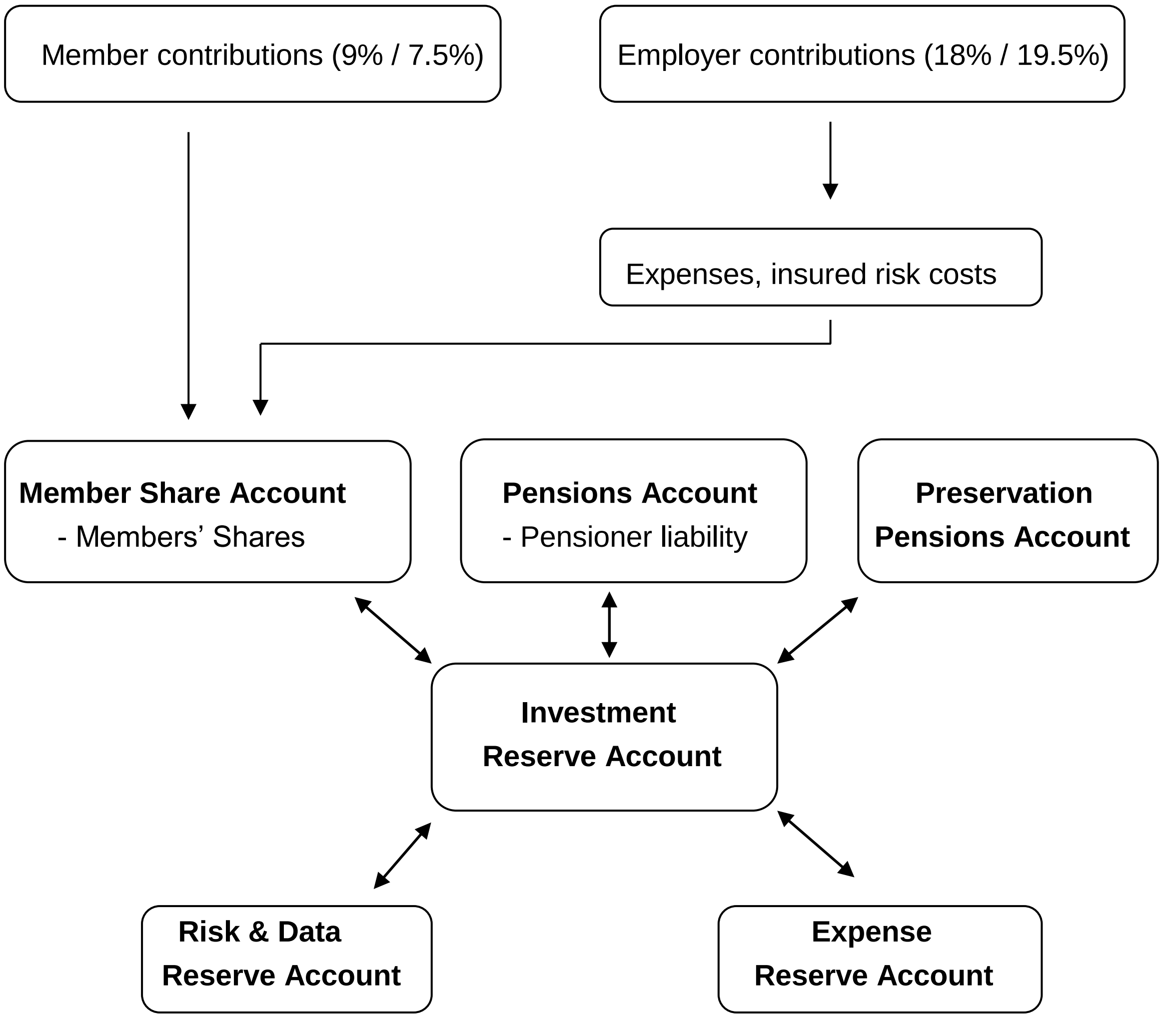
1.1 Summary statistics

	30 June 2014	30 June 2013
Active and deferred members		
Number	37 099	35 506
Annual pensionable salaries (R million)	6 182	5 467
Salary weighted average age (years)	42.7	42.5
Salary weighted average service (years)	8.8	8.7
Pensioners		
Number	725	742
Annual pension (R000)	29 477	28 350
Average pension (R)	40 658	38 207
Pension weighted average age (years)	58.2	56.9

Statistics over the inter-valuation period	**Average % p.a.**
Contribution rates	
- Local Authorities	18.0 / 19.5
- members / Contract Employees	9.0 / 7.5
Investment returns	
- overall investment return on Fund's assets	23.2
- investment returns allocated:	
Growth Portfolio	24.5
Protection Portfolio	6.5
Moderate Portfolio	12.8
- investment return on Pensioner Portfolio	12.4
Salary increases	
- for members in force throughout	6.8
Inflation	
- CPI for year ending 30 June 2014	6.6
Pension increase - effective 1 March 2014	5.5

1.2 Fund structure

The following diagram illustrates the allocation of the member and Local Authority contributions, as well as the structure of the Fund Accounts, as per the Rules:



1.3 Protection Portfolio

The Fund introduced a Protection Portfolio with effect from 1 September 2007. The aim of the Protection Portfolio is to provide protection against market volatility. Members who are older than age 50 may transfer all or part of their Fund Credits to the Protection Portfolio on 1 July of each year. As from 1 January 2010, members of 50 years and older were afforded the option of additional switches in any month of their choice.

The Protection Portfolio assets were invested in money market, bond and bond derivative portfolios as at the valuation date. The rates of investment return declared on the Protection Portfolio Members' Shares are the net investment returns on the Protection Portfolio assets.

1.4 Moderate Portfolio

With effect from 1 July 2011, members over age 50 have the option of investing in the Moderate Portfolio. Members over age 50 years may invest either 50% or 100% of their Member's Share in the portfolio. The assets of the Moderate Portfolio are limited to between 18% and 56% in equity investments and are managed on a "life-stage" basis depending on the member's chosen level of risk.

1.5 Preservation Pension Account

A separate account known as the Preservation Pension Account was established effective 1 September 2009. The purpose of the account is to enable the Fund to accept transfers from a pension fund which allows a maximum commutation of one third of the retirement benefit, whereas the Fund allows full commutation.

Members may allocate part or all of their Preservation Pension Account to the Protection Portfolio or the Moderate Portfolio. Once a member's transfer value has been allocated to the account, no further contributions are added. On retirement, a maximum of one third of the value of the Member's Share in the Preservation Pensions Account may be commuted for a cash lump sum. The balance must be used to purchase an annuity and the member's membership of the Fund ceases after retirement.

1.6 Build-up of the accounts

The Pensions Account has been built up separately since the surplus apportionment date. The account was accumulated with cashflows and net fund returns earned on the assets during each financial year as shown in section 6.2.

The Trustees previously resolved that the net fund return earned on the total pool of assets shall be credited to all accounts. With effect from 1 March 2011, the Fund's investment strategy was reviewed and separate assets are held for the Member Share Account and Pensions Accounts. With effect from 1 March 2011, the return allocated to the Pensions Account is based on the returns earned on the assets underlying the pensioner portfolio.

The Risk & Data Reserve Account applies to both the Share and Pensions Accounts and is available to fund any data corrections in either account. We have built up the Risk and Data Reserve by accumulating the opening balance at the previous valuation with actual net fund returns on the Growth Portfolio.

The Growth Portfolio, Protection Portfolio and Moderate Portfolio accumulate at the net rate of investment return based on the assets underlying each of the portfolios.

1.7 Financial condition

	30 June 2014	30 June 2013
	R 000	R 000
Total value of net assets [1]	17 211 981	13 639 228
Less:		-
Risk reserve Account	(22 345)	(17 941)
Data Reserve Account	(16 782)	(13 474)
Expense Reserve Account [2]	0	0
Balance of net assets	**17 172 854**	**13 607 813**
Pensions Account [3]		
Market value of assets	622 536	577 241
Pensioner liability	(552 784)	(549 369)
Surplus	69 752	27 872
Funding level - Pensions Account	**112.6%**	**105.1%**
Member Share Account		
Assets of the Member Share Account	16 488 416	12 980 423
Members' Shares		
– Growth Portfolio	(15 807 300)	(12 295 406)
– Protection Portfolio	(153 347)	(214 892)
– Moderate Portfolio	(547 815)	(438 700)
Processing Reserve Account	(20 046)	31 425
Funding level Member Share Account	**99.9%**	**100.2%**
Preservation Pension Account [4]		
Assets of the Preservation Pension Account	61 902	50 149
Members' Shares	(61 902)	(50 149)
Surplus	0	0
Funding level Preservation Pension Acc.	**100.0%**	**100.0%**

1. Total value of net assets is based on draft financial statements.
2. The balance of the Expense Reserve Account was transferred to the Processing Reserve Account.
3. The Pensions Account includes a provision for future expected pensioner expenses.
4. The Preservation Pensions Account includes transfers received from other pension funds per Rule 20.

1.8 Processing reserve Account

Excesses or shortfalls in the Processing Reserve Account are expected to arise to the extent that the monthly investment returns declared differ from the actual underlying investment return. The Processing Reserve Account is maintained as close to zero as possible. This may be achieved by allocated the excess or shortfall arising at each annual actuarial valuation to the monthly investment return allocated to Members' Shares. A negative reserve may arise temporarily as part of the process and is not a cause for any concern in the normal course of events.

1.9 Composition of contribution rate

	Total	Option A	Option B	Option C	Option D	Option E	Option F[1]	Option G
Number of members	37 120	15 025	16 332	1 222	2 977	1 395	22	147
% of membership	100%	40.5%	44.0%	3.3%	8.0%	3.8%	0.1%	0.4%
Annual payroll (Rm)	6 170	2 572	2 394	239	699	227	5	35
Contributions as a % of payroll								
Local Auth. Cont. [1]	18.00	18.00	18.00	18.00	18.00	18.00	18.00	18.00
Less:								
Death & disability	(3.45)	(3.00)	(5.00)	(2.00)	-	(3.25)	(3.00)	(0.60)
Funeral expenses [2]	(0.11)	(0.11)	(0.11)	(0.11)	(0.11)	(0.11)	-	(0.11)
Expense allowance [3]	(0.62)	(0.62)	(0.62)	(0.62)	(0.62)	(0.62)	(0.62)	(0.62)
Net Local Authority contribution	13.82	14.27	12.27	15.27	17.27	14.02	14.38	16.67
Plus:								
Member contribution	9.00	9.00	9.00	9.00	9.00	9.00	9.00	9.00
Available for retirement	**22.82**	**23.27**	**21.27**	**24.27**	**26.27**	**23.02**	**23.38**	**25.67**

1. For Contract Employees and Councillors, the Local Authority contribution rate is 19.5% of salary. The member contribution rate for these members is 7.5% of salary. The total member and Local Authority contribution rate of 27% of salary is the same as for other members. New Employees are defined as employees who were employed on contract by the City of Cape Town at the time of joining the Fund or who have been newly employed by the City of Cape Town after 1 August 2006. The Local Authority contribution for these members may change as agreed by SA Local Government Bargaining Council.
2. Funeral expenses are based on a sliding scale depending on each member's salary. The expense represents an average of the overall funeral expense, expressed as a percentage of salary.
3. Expenses are funded based on a sliding scale depending on each member's salary. The expense allowance represents an average of the overall expense funding provision, expressed as a percentage of salary.

The Fund introduced a new risk benefit Option G, effective 1 October 2013. This category provides a basic death benefit of one times annual salary. All members who were in Option D prior to this date were given the opportunity to move to Option G or any other category. With effect from 1 October 2013, Option D was closed for new members under the age of 50 to ensure that all new members have some form of death benefit cover. Members may only elect Option D if they are older than age 50 or a Councillor.

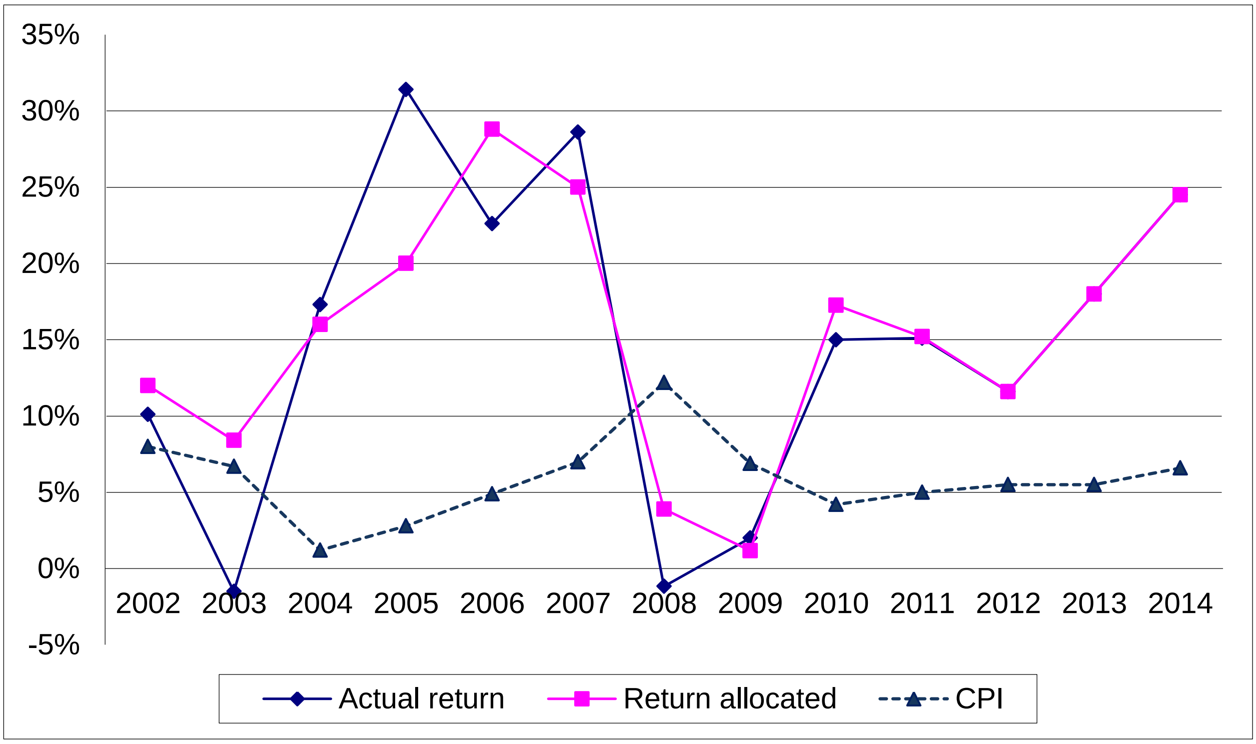
1.10 Investment returns declared

1.10.1 Investment returns allocated over the last five years

Year ending 30 June	Investment return allocated per annum			
	Growth Portfolio	Moderate Portfolio	Protection Portfolio	Pensioner Portfolio
2010	17.3%	-	7.3%	-
2011	15.2%	-	6.6%	3.7%
2012	11.6%	9.2%	7.3%	11.2%
2013	18.0%	11.4%	6.9%	15.2%
2014	24.5%	12.8%	6.5%	12.4%
3 year average	**17.9%**	**11.1%**	**6.9%**	**12.9%**
5 year average	**17.2%**	**-**	**6.9%**	**-**

1.10.2 Growth Portfolio investment returns and inflation

The following graph gives a comparison of Growth Portfolio actual investment returns, returns allocated and CPI inflation since 2002:



1.11 Pension increases

The Fund has invested the assets in respect of the pensioner liabilities in a LDI structure to more closely match the nature of the liabilities. As a result of this, the movement in the assets should more closely follow the movement in the liabilities. We valued both the assets in the Pensions Account and the pensioner liabilities at market related value. The funding level of the Pensions Account increased from 105.1% to 112.6% during the inter-valuation period. In view of the sound financial condition of the Pensions Account at the valuation date a pension increase of up to 6.6% (100% of year on year CPI inflation to June 2014) effective 1 March 2015 can be recommended.

Historically, the Board has granted pensioners adhoc bonuses. A bonus of 100% of monthly pension was paid to pensioners in December 2013. The Pensioner Account is sufficient to provide for a 100% bonus in December 2014.

1.12 Conclusions

- Investment returns of 24.5% p.a. on average were awarded on Members Shares in the Growth Portfolio. The return of 24.5% p.a. represents a real return of 17.9% p.a. relative to CPI inflation of 6.6% p.a. for the year under review. The total interest rate allocated since 1 May 1996, the date of inception of the portfolio, is 15.9% p.a. on average compared to CPI inflation of 6.4% p.a., providing an excellent real return of 9.5% p.a. since inception of the Fund.

- Investment returns of 6.5% p.a. on average were awarded on Members Shares in the Protection Portfolio. The return of 6.5% p.a. represents a real return of -0.1% p.a. relative to CPI inflation of 6.6% p.a. for the year under review. The total interest rate allocated since 1 September 2007, the date of inception of the portfolio, is 8.5% p.a. on average compared to CPI inflation of 6.7% p.a., providing a real return of 1.8% p.a. since inception of the Protection Portfolio.

- The Moderate Portfolio was introduced in July 2011. Investment returns of 12.8% p.a. on average were awarded on Members' Shares in the Moderate Portfolio. The return of 12.8% p.a. represents a real return of 6.2% p.a. relative to CPI inflation of 6.6% p.a. for the year under review. The total interest rate allocated since 1 July 2011, the date of inception of the portfolio, is 11.1% p.a. on average compared to CPI inflation of 5.9% p.a., providing a real return of 5.2% p.a. since inception of the Moderate Portfolio.

- The Processing Reserve Account amounted to -0.13% of Members' Shares in the Growth Portfolio at 30 June 2014. The reserve accounts for minor differences in the timing of cashflows and differences in the actual net fund return earned relative to returns allocated to Members' Shares.

- The risk benefits for active members are fully reinsured. Part of the post retirement death benefit is self-insured. The self-insurance and reinsurance arrangements are appropriate in view of the size and nature of the Fund.

1.13 Recommendations

I recommend the following:

- an annual pension increase of up to 6.6% (100% of CPI) effective 1 March 2015
- pro-rata increases for pensions in payment for less than one year
- that the investment return allocated to Members' Shares in the Growth Portfolio is decreased by 0.13% as part of the monthly investment return allocation.

1.14 Certification

An investigation of the investment strategy of the Cape Retirement Fund for Local Government was undertaken at the current valuation. I certify that, in my opinion, the structure of the assets is appropriate relative to the nature of the liabilities, given normal circumstances.

I certify that in my opinion:

- The Fund is in a sound financial condition as the valuation date after allowing for an adjustment of -0.13% to Members' Shares.
- The nature of the assets is suitable for the Fund.
- The assets are appropriately matched relative to the term and nature of the liabilities of the Fund.
- The Fund's investment strategy is suitable.
- The active member risk benefits are fully re-insured. I consider this to be appropriate for the Fund.

The next statutory actuarial valuation will be performed as at 30 June 2015.

Sean Neethling BSc CFP® FIA FASSA
Fellow of the Actuarial Society of South Africa
in my capacity as an employee of
Momentum Specialised Solutions

The Actuarial Society of South Africa is my primary regulator.
2 March 2015

Section 2 Introduction

2.1 Overview

This report is addressed to the Trustees of the Cape Retirement Fund for Local Government and contains the results of the financial review as at 30 June 2014.

The previous statutory actuarial valuation of the Fund was carried out as at 30 June 2013. The period between the previous and the current valuation dates is referred to as the inter-valuation period.

The Cape Retirement Fund for Local Government was established with effect from 1 May 1996 when members of the Cape Joint Pension Fund were given the option to transfer the value of their accrued benefits to the Cape Retirement Fund.

In the period from 1 May 1996 to 30 May 1997, a total of approximately 18 535 members transferred from the Cape Joint Pension Fund to the Cape Retirement Fund for Local Government.

2.2 Objectives of the actuarial valuation

The main objectives of the actuarial valuation are to:

- determine the financial condition of the Pensions Account and Member Share Account by comparing the value of assets to the value of liabilities
- determine the level of any reserve accounts
- assess the allocation of contributions between retirement benefits, risk benefits and expenses
- review the investment returns allocated to active and deferred members
- recommend the level of pension increases for pensioners
- examine the impact of any changes during the inter-valuation period.

2.3 Data

The membership and asset data required for the valuation was supplied by Verso Financial Services (Pty) Ltd, including audited accounts. The data has been examined for accuracy and reasonability and has been accepted for the purposes of the valuation.

Section 3 Developments since the previous valuation

The following section describes developments since the previous statutory actuarial valuation as at 30 June 2013 including all rule amendments since the Revised Rules were registered.

3.1 Contribution rates

Local Authorities and members contributed at a rate of 18% and 9% of pensionable salaries respectively. The number of Contract Employees with member and Local Authority contribution rates of 7.5% and 19.5% respectively increased from 222 to 551 over the inter-valuation period.

3.2 Rule amendments

The Revised Rules were amended as follows:

Rule amendment 1 effective 1 October 2013. Include a new risk option category G from 1 October 2013 which provides a basic and inexpensive level of risk benefit cover. Risk option D has been closed from 1 October 2013 for all new members under age 50 years who join the Fund to ensure that all new members have some form of death benefit cover. Existing members in category D will be given a once-off option to elect to change to another risk option category. Councillors, due to the nature of their appointment, will be allowed to belong to category D.

Rule amendment 2 effective 1 March 2014:

- amends the reference in the rules relating to the office of a trustee becoming vacant due to a breach of the code of conduct, or in respect of a trustee / potential trustee not meeting specific fit and proper requirements to also apply at the time of the trustee elections and the potential trustee at that time not complying with the trustee code of conduct.
- amends the reference to sub-committees to include the formation of ad-hoc committees which are established for a specific short-term purpose.
- amends the reference of Investment Reserve Account throughout the rules to the Processing Reserve Account.
- amends the Participating Employer contribution rate in respect of councillors to comply with the legislation that is applicable to councillors in terms of the Pension Benefits for Councillors of Local Authorities Act 105 of 1987 read with the Determination of Upper Limits of Salaries, Allowances and Benefits of Different Members of Municipal Councils as gazetted.

Rule amendment 3 effective 1 June 2014. The rules were amended to make special provision for the terms on which a councillor may join or exit from the Fund.

3.3 Pension increases

Pensions in payment were increased by 5.5% on 1 March 2014.

Pro-rata increases were applied for pensions in force for less than one year.

An ad hoc pensioner bonus of 100% of monthly pension was granted to pensioners in December 2013.

3.4 Monthly investment return allocations

Previously, the Fund operated a smoothed investment return rate approach. The Trustees resolved to implement monthly investment returns based on actual net fund returns with effect from 1 December 2008.

Investment returns of 24.5% p.a. were awarded for the year ending 30 June 2014 on the Growth Portfolio.

Investment returns of 6.5% p.a. were awarded for the year ending 30 June 2014 on the Protection Portfolio.

Investment returns of 12.8% p.a. were awarded for the year ending 30 June 2014 on the Moderate Portfolio.

3.5 Preservation Pensions Account

A separate account known as the Preservation Pensions Account was established effective 1 September 2009 . The purpose of the account is to enable the Fund to accept transfers from a pension fund which allows a maximum commutation of one third of the retirement benefit, whereas the Fund allows full commutation.

Members may allocate part or all of their Preservation Pension Account to the Protection Portfolio or the Moderate Portfolio. Once a member’s transfer value has been allocated to the account, no further contributions are added. On retirement, a maximum of one third of the value of the Member’s Share in the Preservation Pensions Account may be commuted for a cash lump sum. The balance must be used to purchase an annuity and the member’s membership of the Fund ceases after retirement.

Section 4 Membership statistics

4.1 Active service and deferred membership

Membership reconciliation	Males	Females	Total
30 June 2013	**21 888**	**13 618**	**35 506**
Adjustments	(62)	(30)	(92)
plus new entrants	2 135	1 402	3 537
less: Retirements	(338)	(165)	(503)
Resignations/ Retrenchments	(650)	(466)	(1 116)
Disabilities	(46)	(11)	(57)
Deaths	(135)	(41)	(176)
30 June 2014	**22 792**	**14 307**	**37 099**
Salary weighted average age (years) [1]			
30 June 2013	43.9	40.4	42.5
30 June 2014	44.0	40.6	42.7
Salary weighted average service (years) [1]			
30 June 2013	9.4	7.6	8.7
30 June 2014	9.5	7.9	8.8
Annual pensionable salary (R'000) [1]			
30 June 2013	3 363 879	2 103 589	5 467 468
30 June 2014	3 779 240	2 402 449	6 181 689

1. Excludes deferred members.

4.2 Pensioners

	Normal / Early	Disabled	Spouses	Children	Total
Pensioner reconciliation					
30 June 2013	**115**	**194**	**294**	**139**	**742**
adjustments					
Plus retirements	2			2	4
dependants			6		6
less cessations	(5)	(6)	(2)	(14)	(27)
30 June 2014	**112**	**188**	**298**	**127**	**725**
Annual pension (R 000)					
30 June 2013	3 213	13 452	10 400	1 337	28 402
30 June 2014	3 483	13 710	11 026	1 258	29 477
Average pension (R)					
30 June 2013	27 941	69 338	35 374	9 620	38 278
30 June 2014	31 104	72 923	36 999	9 904	40 658
Pension weighted average age (years)					
30 June 2013	69.1	57.5	57.4	18.1	58.8
30 June 2014	69.8	61.1	59.7	17.9	61.6

[1] Total pension weighted average ages exclude children.

Section 5 Assets

5.1 Total value of assets

For the purpose of the valuation, certain adjustments are made to the Fund's market value in order to take account of current assets and current liabilities as at the valuation date. These adjustments, taken from the financial statements, are as follows:

	R 000
Market value of assets	**17 301 372**
Plus: sundry debtors	
Arrear contributions	78 520
Accounts receivable	34 339
Transfers receivable	-
Cash at bank	134 018
Less: sundry creditors	
Benefits due	(290 875)
Unclaimed benefits	(209)
Accounts payable	(45 184)
Total net assets	**17 211 981**

A consolidated income statement is given in Appendix B.

5.2 Market value of assets

As at the valuation date, the Fund's assets were divided amongst a number of investment managers and direct investments as follows:

30 June 2014	Market value R 000	% of total
Coronation Asset Management (Pty) Ltd	3 810 406	22.0
Allan Gray South Africa (Pty) Ltd	3 273 851	18.9
Stanlib Asset Management Ltd	1 307 714	7.6
Investec Asset Management (Pty) Ltd	2 531 214	14.6
Sanlam Investment Management (Pty) Ltd	2 592 525	15.0
Verso Multi Manager (Pty) Ltd	972 161	5.6
Kagiso Asset Management (Pty) Ltd	598 121	3.5
Peregrine Equities (Pty) Ltd	207 030	1.2
PIMCO Europe Ltd	-	0.0
Aberdeen Asset Managers Ltd	751 636	4.3
Old Mutual Global Index Trackers(Pty) Ltd, trading as Dibanisa Fund Managers	754 443	4.4
All Seasons Capital Management Ltd	483 268	2.8
Other	19 003	0.1
Total market value	**17 301 372**	**100.0**

5.3 Asset mix

As at the valuation date, the investments were allocated amongst the various asset classes as follows:

Asset class	Asset allocation
Domestic equities	42%
Bonds, debentures and loans	23%
Cash	11%
Foreign investments	24%
Alternative investments	0%

5.4 Investment strategy

The investment strategy of the Fund is detailed in the Fund's investment policy document.

For the active members, the Fund offers members a choice of three investment strategies (the Growth Portfolio, the Moderate Portfolio and the Protection Portfolio) to cater for the changing risk appetites of typical members over their working lifetime.

The strategic asset allocation of the Growth Portfolio was as follows:

Class	**Strategic position**
Equities	63.5%
Bonds	22.5%
Cash	6.0%
Property	8.0%

The return objective for the Growth Portfolio is to earn a positive real return of 4% p.a. (net of investment charges and tax) over rolling three-year periods. A shorter-term objective is to avoid possible downside risk. The Fund employs hedging strategies towards meeting this objective.

The assets of the Fund are invested in a diversified portfolio of cash, property, equities and fixed interest investments. Assets are held offshore as permitted by Regulation 28 of the Pension Funds Act.

Performance of the various asset managers is monitored over 12-month rolling periods and measured over rolling three-year periods.

With effect from 1 July 2011, members over age 50 have the option of investing in the Moderate Portfolio. The assets of the Moderate Portfolio are limited to between 18% and 56% in equity investments and are managed on a "life-stage" basis depending on the member's chosen level of risk. The return objective for the Moderate Portfolio is to earn a positive real return of 3% p.a. over rolling three-year periods.

The Protection Portfolio is aimed at providing protection against market volatility. The objective of this portfolio is to provide returns in excess of cash (as measured by the Short Term Fixed Interest benchmark), whilst protecting the value of capital invested over any three-month rolling period. The Protection Portfolio has a conservative risk profile with no exposure to equity.

The Trustees have set a separate investment strategy for the pensioner assets so as to better match the liability profile of this group of members.

5.5 Regulation 28

Regulation 28 was amended on 22 February 2011 effective 1 July 2011. The amended regulation sets out limits on the assets that may be held in various categories. The regulation contains important principles that the Trustees must apply.

The Investment Policy Statement must be reviewed at least annually taking Regulation 28 into account.

5.6 Matching of assets and liabilities

Account should be taken of the long term nature of the Fund. The Member Share Account should be matched largely by investments in equities and property to protect against the erosion of real values by inflation. The Pensions Account should be underpinned by greater exposure to bonds and cash. Prudence also requires a spread of investments over sectors, industries and geographic locations.

With effect from 1 March 2011, the Fund's investment strategy was reviewed and separate assets are held for the Share and Pensions Accounts. The Trustees decided to follow a Liability Driven Investment (LDI) strategy and appointed Sanlam Investment Management as the asset manager.

The assets of the Fund are invested according to these principles and, in my opinion, the assets represent a suitable mix of asset classes relative to the term and nature of the liabilities of the Fund.

Section 6 Pensions Account

6.1 Defined benefit obligation underpinned by ring-fenced value of assets

The pensioner liability represents a defined benefit obligation in the Fund. The value of the assets available to support the pensioner liability has been ring-fenced in the Pensions Account. The funding level of the Pensions Account can be determined by comparing the actuarial value of the assets accumulated in the Pensions Account to the present value of the pensioner liabilities (including all pension increases to date).

The Trustees previously resolved not to specify a separate asset mix to underpin the Pensions Account, although the *value* of the assets has been ring-fenced in the Pensions Account. With effect from 1 March 2011, the Fund reviewed the investment strategy thereby separating the assets underlying the Pensions Account and structuring the assets to achieve a closer match with the liabilities. The Pensions Account has since been accumulated with the investment return earned on the underlying pensioner assets.

6.2 Market value of assets of the Pensions Account

The Pensions Account was accumulated with net investment returns over the inter-valuation period as follows:

	R 000
Pensions Account at 30 June 2013	**577 241**
Less: Pension payments	(30 805)
Pension expenses	(1 101)
Plus: Retirements (transfers from Member Share Account)	3 750
Reinsurance recoveries	3 603
Investment returns	69 848
Pensions Account at 30 June 2014	**622 536**

6.3 Actuarial value of assets of the Pensions Account

The method and long term assumptions used to value the assets and the liabilities of the Pensions Account should be consistent.

At the previous valuation date, the actuarial value of the assets of the Pensions Account was been determined by discounting the expected future income streams generated by a notional portfolio of assets at the valuation rate of interest. This method smooths out short-term fluctuations in the market value of the assets and aims to achieve consistency between the actuarial value of the assets and the value of the liabilities.

Since then, the Board has implemented a separate investment strategy for the pensioner assets to better match the movement of the liabilities.

Thus, for the purpose of this valuation, we have revised our methodology by valuing both the pensioner assets and liabilities at market value. Whilst the market value of the assets is typically more volatile than a long-term actuarial valuation, the funding level of the Pensions Account should be more stable over the long-term.

6.4 Pensioner liability

The pensioner liability, based on a target annual pension increase of 100% of CPI, is as follows:

Pensioner liability	30 June 2014 R 000	30 June 2013 R 000
Disabilities	249 345	251 273
Retirements	54 394	50 893
Spouses	224 509	220 465
Children	4 639	6 428
Pensioner expense	19 897	20 310
Total	**552 784**	**549 369**

6.5 Disabled pensioners

In terms of the previous disability benefit structure, the pension for disabled pensioners was determined as the Expected Pension subject to a minimum of 50% (or 75% for specific causes of disability) of salary at date of disability. The Expected Pension is the pension that the disabled pensioner would have received at normal retirement age 65, based on a notional projection of the Member's Share accumulated with notional future contributions to age 65.

The minimum disability pension (50% or 75% of salary) was insured with Sanlam and Momentum. The insurers pay the "Insured Pension" to the Fund on a monthly basis. Insured Pension payments cease at age 65 or on earlier termination in terms of the insurance contract (e.g. recovery from disability). If the pension in payment to the disabled pensioner exceeds the Expected Pension, then the pension reduces to the Expected Pension at age 65.

The disability pension and Expected Pension increase with the annual pension increases granted by the Trustees. The Insured Pension increases by 5% each year.

6.6 Actuarial valuation method

The pensioner liability is calculated as the actuarial present value of future pension payments, including an allowance for future pension increases according to the pension increase policy of the Fund.

The disabled pensioner liability is determined as:

- the present value of the Current Pension to age 65 and the Expected Pension thereafter
- ***less***: the present value of the Insured Pension to age 65

6.7 Actuarial assumptions

The current and previous actuarial valuation assumptions are as follows:

Assumption	30 June 2014	30 June 2013
Interest rate	9.04% p.a.	7.79% p.a.
Pension increases	6.78% p.a.	5.66% p.a.
Interest rate net of pension increases	2.11% p.a.	2.02% p.a.
Price inflation	6.78% p.a.	5.66% p.a.
Mortality tables		
Pensioners	PA(90) – 2 years with 1.5% p.a. improvement.	PA(90) – 2 years with 1.5% p.a. improvement
Disability pensioners (Current Pension)	PA(90) + 2 years with 1.5% p.a. improvement.	PA(90) + 2 years with 1.5% p.a. improvement
Decrement rates for the insured disability pension	GLTD[1] rates with a 3 month waiting period.	GLTD[1] rates with a 3 month waiting period
Husband's age greater than wife	4 years	4 years
Proportion married	90%	90%

[1] Group Long Term Disability

6.8 Principles underlying the best estimate valuation basis

PF 117 issued by the FSB in July 2004 requires liabilities to be calculated at the surplus apportionment date on 'best estimate' assumptions. We have carried this principle through to the current valuation.

Valuation rate of interest

The expected long term valuation interest rate is derived with reference to the yields on government bonds of appropriate duration. The valuation rate of interest reflecting these yields reduced from 7.79% to 8.51% p.a. at 30 June 2014, based on the nominal bond yield at a duration of 9 years.

Price inflation

The Reserve Bank targets an inflation rate in the range of 3% to 6% p.a. At the previous valuation date, the "gap" between the valuation rate of interest and the price inflation assumption was 2.13% p.a. However, as the real investment yields on Index Linked Bonds continue to reduce, a lower long term real return assumption and higher price inflation assumption is considered to be more appropriate. The assumed rate of price inflation was set equal to the difference between the valuation rate of interest less a 0.5% p.a. adjustment for inflation risk premium (9.04% - 0.5% i.e. 8.54% p.a.) and the real yield on index linked bonds at a duration of 9 years (1.76% p.a.) i.e. 6.78% p.a.

Pension increases

The pension increase target is 100% of price inflation 6.78%. The post retirement interest rate (i.e. the valuation interest rate net of the allowance for pension increases) decreased from 2.02% p.a. to 2.11% p.a.

Post- Retirement Mortality

Continuing improvement is expected in the longevity of pensioners. Insurers generally are using the PA(90) table rated down by two years, plus an additional percentage annual allowance for improvement. We assumed that pensioner life expectancies will improve by 1.5% p.a. annum in future.

6.9 Pension increase policy

In the light of inflation, the position of pensioners needs continuing sympathetic consideration. The following sections discuss the main issues pertaining to pension increases.

The Rules of the Fund state that pensions may be increased from time to time at a rate determined by the Trustees in consultation with the Actuary. The Trustees may also grant ad-hoc bonuses to pensioners.

The Pension Funds Second Amendment Act (the Act) requires the Trustees to state a pension increase policy as a percentage of a measure of inflation, and to communicate to pensioners whenever it is changed. The Act also provides for minimum pension increases to be reviewed at least every three years.

The pension increase policy of the Fund is as follows:

- Annually perform a review to target a pension increase of 100% of CPI effective 1 March but based on CPI to the preceding 30 June (subject to affordability);

- Every three years perform a catch-up review to increase pensions to 100% of CPI since the date of retirement, subject to the value of the notional pensioner account and affordability, as set out in the Pension Funds Second Amendment Act.

6.10 Past pension increases

The history of pension increases granted by the Trustees is as follows:

Increase date as at 1 March	Pension increase %	CPI % to previous 30 June
1997	5.15	6.86
1998	8.79	8.79
1999	4.50	5.15
2000	8.00	7.25
2001	8.50	5.16
2002	7.00	6.31
2003	7.00	8.00
2004	1.70	6.71
2005	5.00	1.23
2006	3.50	2.82
2007	4.80	4.90
2008	7.00	6.40
2009[1]	11.60	12.20
2010[2]	7.50	6.90
2011	4.20	5.00
2013	5.00	5.50
2014	5.50	6.60
Average	**6.10**	**6.16**

1. Inflationary catch-up increases were granted on 1 March 2008 after taking account of the 7% p.a. increase.
2. Implemented on 1 January 2010.

Pro-rata pension increases applied for pensions in payment for less than one year.

6.11 Pensioner bonuses

Ad-hoc pensioner bonuses have been granted as follows:

Month	Bonus as a % of monthly pension
November 2009	100%
February 2011	100%
December 2011	100%
December 2013	100%

Pro-rata bonuses applied for pensions in payment for less than one year.

6.12 Financial condition and pension increase affordability

The financial condition of the Pensions Account is as follows:

Pensions Account	30 June 2014 R 000	30 June 2013 R 000
Value of assets (market value)	622 536	577 241
Pensioner liability	(552 784)	(549 369)
Surplus	69 752	27 872
Funding level	**112.6%**	**105.1%**

The Funding level increased from 105.1% to 112.6% in the Pensions Account during the inter-valuation period. In view of the financial condition of the Pensions Account at the valuation date, a pension increase of up to 6.6% (100% of CPI) effective is affordable.

The Trustees granted an increase of 5.5% effective 1 March 2014, pro rata for pensions in payment for less than one year.

A pensioner bonus of 100% of monthly pension was granted in December 2013.

Section 7 Reserve Accounts

7.1 Risk Reserve Account

Risk benefits for active members are fully reinsured. The reinsurance arrangements are appropriate in view of the defined contribution nature of the active member liabilities. The Trustees have resolved to pass the full risk of increasing death and disability costs on to members, and not to hold any additional reserves to cushion the effect of future increases from causes such as HIV/AIDS. This is consistent with the Trustees' philosophy that the Fund's overriding function is to provide retirement benefits.

The Risk Account has been established:

- to absorb the impact of adverse experience in the uninsured risk benefits
- to account for any excess or shortfall in reinsurance payments to the Fund relative to insured death benefits.

The Risk Reserve Account was accumulated over the inter-valuation period as follows:

Risk Reserve Account	**R 000**
Balance as at 30 June 2013	**17 941**
Investment returns	4 404
Balance as at 30 June 2014	**22 345**

The Risk Reserve Account accumulated to R22.3 million at the valuation date, representing 0.13% of the total assets of the Fund.

7.2 Data Reserve Account

The Data Reserve Account absorbs strains caused by data errors and other unforseen contingencies.

The Data Reserve Account was accumulated with investment returns as follows:

Data Reserve Account	**R 000**
Balance as at 30 June 2013	**13 474**
Investment returns	3 308
Balance as at 30 June 2014	**16 782**

The Data Reserve Account accumulated to R16.8 million at the valuation date, representing 0.10% of the total assets of the Fund.

7.3 Investment Reserve Account

The purpose of the Investment Reserve Account was originally to absorb fluctuations in the market value of the fund's investments and thus smooth investment returns allocated to Members' Shares.

The Investment Reserve Account is now maintained close to zero by allocating any excess or shortfall in the accountant to Members' Shares. Actual investment returns are allocated to Members' Shares each month. The reserve essentially acts as a processing error reserve to account for mismatches and timing differences between the investment returns earned on the Fund's assets the returns allocated to Members' Share Accounts.

A build up of the account over the inter-valuation period is as follows:

Investment Reserve Account	**R 000**
Balance as at 30 June 2013	**31 425**
Investment returns earned	3 200 968
Interest allocated to Share Account	(3 253 242)
Transfer from the Expense Reserve Account	803
Balance as at 30 June 2014	**(20 046)**

Appendix A Summary of financial structure and benefits

A.1 Financial structure *(subject to registration of rule amendments 6 and 7)*

The Rules provide for the assets of the Fund to be held in the following accounts:

- **Member Share Account**, comprising the sum of Members' Shares
- **Pensions Account**, held in respect of all pensions in payment to pensioners
- **Investment Reserve Account**, to account for differences between actual net Fund returns and the monthly investment returns awarded on Members' Shares and the returns allocated to the Pensions Account and the various Reserve Accounts
- **Risk and Data Reserve Account**, to absorb the impact of adverse experience in uninsured risk benefits and absorb strains caused by data errors and unforseen contingencies
- **Expense Reserve Account**, to meet the cost of insured risk benefits and ongoing Fund expenses
- **Preservation Pension Account**, to receive benefits from a Pension Fund.

Member Share Account	
Credits	**Debits**
Transfer Values and Member contributions.	Negative investment earnings.
Local Authority contributions towards retirement benefits.	Lump sum benefits paid to a Member or benefits transferred to an Insurer.
Additional voluntary contributions.	Transfers to the Pensions Account of the balance of the Member's Share after the payment of any lump sum on retirement.
Investment earnings.	
Additional amounts payable by the Local Authority for exiting members.	Settlement of housing loans.
Special transfers from the Investment Reserve Account.	Payment of pension interest on divorce, maintenance or court order.
Transfers from the Risk and Data Reserve Account in respect of reinsured lump sum death and disability income benefits.	Amounts transferred to the Risk and Data Reserve Account due to changes to Member data.

Pensions Account	
Credits	**Debits**
Opening balance.	Pension payments.
Transfers from the Member Share Account to purchase pensions on retirement.	Cash value of death after retirement benefit of excess of Member's Share over total benefits paid.
Transfers from the Risk and Data Reserve Account in respect of reinsured disability income benefits.	Cash value of death after retirement during the 5 year guarantee period benefit.
Investment earnings from the Investment Reserve Account.	Transfer to the Expense Reserve Account in respect of pensioner expenses.
Contributions from the Local Authority to eliminate any actuarial shortfall in the Pensions Account.	Negative investment earnings.
	Amounts transferred to the Risk and Data Reserve due to changes to pensioner data.

Investment Reserve Account	
Credits	**Debits**
All investment earnings of the Fund.	Investment returns transferred to the: • Member Share Account • Pensions Account • Risk and Data Reserve Account • Preservation Pension Account.
Transfers from the Member Share Account to clear any deficit in the Investment Reserve Account.	Any other payments by the Fund not specified elsewhere in the Rules.
Transfers of negative investment earnings from the Preservation Pension Account and Pensions Account.	
Transfer of any positive balance of the Expense Reserve Account at the end of each Fund Year.	
Any other income attributable to the Fund.	

Risk and Data Reserve Account	
Credits	**Debits**
Reinsurance recoveries from an Insurer. Investment returns. Transfers from the Member Share Account and the Pensions Account due to changes in member and pensioner data.	Transfers to the Member Share Account in respect of reinsured lump sum death and disability benefits. Transfers to the Pensions Account in respect of reinsured disability income benefits. Transfers to the Member Share Account and the Pensions Account due to changes in member data.

Expense Reserve Account	
Credits	**Debits**
Local Authority contributions allocated towards insured risk benefits and the amount determined to cover Fund expenses. Transfers from the Pensions Account in respect of pensioner expenses.	All risk benefit premiums payable to the Insurers for the reinsurance of the insured risk benefits. All costs and expenses incurred by the Fund. At the end of each Fund Year, any remaining balance whether positive or negative shall be allocated to the Investment Reserve Account.

Preservation Pension Account	
Credits	**Debits**
Members' benefits transferred from a Pension Fund. Investment returns.	Negative investment returns. Lump sum benefits paid. Transfers to an Insurer to purchase an annuity. Settlement of housing loans or housing loan guarantees. Payment of any divorce benefit or court order.

A.2 Contributions

	Percentage of annual pensionable salary		
	Member	**Local Authority**	**Total**
Members	9.00%	18.00%	27.00%
Contract Employees and Councillors	7.50%	19.50%	27.00%

New Employees are defined as employees who were employed on contract by the City of Cape Town at the time of joining the Fund or who have been newly employed by the City of Cape Town after 1 August 2006. The definition of New Employee also includes all Employees employed by any Local Authority and who elect to join the Fund from 1 January 2007 (excluding Contract Employees). The Local Authority contribution for New Employees may change as agreed by SA Local Government Bargaining Council.

The costs of insured risk benefits and Fund expenses are deducted from the Local Authority's contributions. The balance is applied towards members' retirement benefits.

A.3 Member's Share

The sum of:

- any transfer value received by the Fund on behalf of members;
- contributions paid by the Local Authority in respect of retirement benefits and contributions paid by members;
- investment return on the above decided upon by the Trustees in consultation with the Actuary, having regard to the investment yield achieved by the Fund.

A.4 Retirement benefit

A pension at date of retirement based on the amount of the Member's Share at that date, subject to:

- any commutation paid;
- allowance for regular increases in pension after retirement;
- allowance for death benefits after retirement.

All pensions may be commuted in full or purchased from an external insurer.

The normal retirement age is 60 years. However members may retire early from age 50 (consent of the Local Authority is required for retirement after age 65). Member and Local Authority contributions are payable up to the retirement date and the benefit is calculated as for normal retirement. New Employees may not retire later than age 60 years except where their contracts of Service state otherwise.

A.5 Disability benefits

Option A	Option B	Option C	Option D	Option E (effective 1 October 2009)	Option F* (effective 1 Sept 2011)
A lump sum that can be purchased with the balance of 3% of salary after deducting the cost of the lump sum death benefit plus Member's Share.	A lump sum that can be purchased with the balance of 5% of salary after deducting the cost of the lump sum death benefit plus Member's Share.	A lump sum equal to Member's Share.	A lump sum equal to Member's Share.	Income disability benefit of 75% of annual pensionable salary, subject to a maximum of R110 000 per month.	A lump sum equal to Member's Share.

With effect from 1 July 2008, the insured lump sum disability benefit reduces by 1/120 per month in the last ten years prior to age 65.

A.6 Death in service

Option A	Option B	Option C	Option D	Option E (effective 1 Oct 2009)	Option F* (effective 1 Sept 2011)
A lump sum that can be purchased with the balance of 3% of salary after deducting the cost of the lump sum disability benefit plus Member's Share.	A lump sum that can be purchased with the balance of 5% of salary after deducting the cost of the lump sum disability benefit plus Member's Share.	A lump sum that can be purchased with 2% of salary plus Member's Share.	A lump sum equal to Member's Share.	A lump sum of 4 times annual pensionable salary plus Member's Share.	A lump sum that can be purchased with 3% of salary plus Member's Share.

* Category F participation applies to members between the ages of 65 and 75 years.

A.7 Death after retirement benefits

Death within 5 years of retirement: the pension will continue until 60 monthly instalments have been paid.

Death after 5 years: 60% spouse's pension plus 10% child's pension up to a maximum of three children. If no spouse's pension is payable, the child's pension is doubled.

Minimum guarantee: The total of all pension payments will not be less than the Member's Share transferred to the Pensions Account at retirement.

A.8 Withdrawal benefit

The full Member's Share is payable, which may be taken in cash or preserved.

A.9 Redundancy, retrenchment or compulsory early retirement benefit

Member's Share;

plus an amount payable by the Local Authority being the lesser of:

- (65 - age nearest birthday) x 8% x Member's Share
- Member's Share.

New Employees do not qualify for the additional amount payable by the Local Authority except where this is specified in their contracts of Service.

A.10 Expenses

Expenses relating to the management and administration of the Fund are borne by the Fund.

Appendix B Summary of accounting transactions

A consolidated income statement for the year ending 30 June 2014 is as follows:

	R 000	R 000
Net assets as at 30 June 2013		**13 639 228**
Income		**5 018 787**
Contributions received and accrued	1 646 729	
Reinsurance recoveries	162 074	
Transfers received	9 016	
Other income	2 362	
Investment income	3 198 606	
Less : Expenditure		**(267 837)**
Administration	(54 612)	
Reinsurance premiums	(213 225)	
Less : Benefit payments and transfers		**(1 178 197)**
Net assets as at 30 June 2014		**17 211 981**

Appendix C History of interest rates versus inflation

Growth Portfolio	% p.a.		
Period	**Investment return allocated**	**CPI**	**Real return**
01/05/1996 - 30/06/1996	17.0	6.9	10.1
01/07/1996 - 30/06/1997	17.0	8.8	8.2
01/07/1997 - 30/06/1998	8.0	5.2	2.8
01/07/1998 - 30/06/1999	10.0	7.2	2.8
01/07/1999 - 30/06/2000	18.0	5.2	12.8
01/07/2000 - 30/06/2001	19.9[1]	6.3	13.6
01/07/2001 - 30/06/2002	12.0	8.0	4.0
01/07/2002 - 30/06/2003	8.4	6.7	1.7
01/07/2003 - 30/06/2004	16.0	1.2	14.8
01/07/2004 - 30/06/2005	20.0	2.8	17.2
01/07/2005 - 30/06/2006	28.8[2]	4.9	23.9
01/07/2006 - 30/06/2007	25.0	7.0	18.0
01/07/2007 - 30/06/2008	3.9	12.2	(8.3)
01/07/2008 - 30/06/2009	1.2	6.9	(5.7)
01/07/2009 – 30/06/2010	17.3	4.2	13.1
01/07/2010 – 30/06/2011	15.2	5.0	10.2
01/07/2011 – 30/06/2012	11.6	5.5	6.1
01/07/2012 – 30/06/2013	18.0	5.5	12.5
01/07/2012 – 30/06/2013	24.5	6.6	17.9
Average since inception:			
01/05/1996 - 30/06/2014	**15.9**	**6.4**	**9.5**

1. Includes a 10% ad-hoc bonus granted on 1 April 2001.
2. Includes a 20% ad-hoc bonus granted on 31 March 2006.

The Fund introduced a Protection Portfolio on 1 September 2007. The investment returns allocated to the Protection Portfolio were as follows:

Protection Portfolio	**% p.a.**		
Period	**Investment return allocated**	**CPI**	**Real return**
01/09/2007 - 30/06/2008	11.6[1]	12.2	(0.6)
01/07/2008 - 30/06/2009	11.7	6.9	4.8
01/07/2009 – 30/06/2010	7.3	4.2	3.1
01/07/2010 – 30/06/2011	6.6	5.0	1.6
01/07/2011 – 30/06/2012	7.3	5.5	1.8
01/07/2012 – 30/06/2013	6.9	5.5	1.4
01/07/2012 – 30/06/2013	6.5	6.6	(0.1)
Average since inception:			
01/09/2007 - 30/06/2014	**8.5**	**6.7**	**1.8**

1. Annualised return for the 10-month period ending 30 June 2008.

The Fund introduced a Moderate Portfolio on 1 July 2011. The investment returns allocated to the Moderate Portfolio were as follows:

Moderate Portfolio	**% p.a.**		
Period	**Investment return allocated**	**CPI**	**Real return**
01/07/2011 – 30/06/2012	9.2	5.5	3.7
01/07/2012 – 30/06/2013	11.4	5.5	5.9
01/07/2013 – 30/06/2014	12.8	6.6	6.2
Average since inception:			
01/07/2011 - 30/06/2014	**11.1**	**5.9**	**5.3**

Appendix D Analysis of change in financial condition

The change in the financial condition of the Pensions Account was analysed as follows:

	R000
Surplus as at 30 June 2013	**27 872**
1. Interest on opening surplus	2 171
2. Change of basis	7 403
3. Investment returns	31 499
4. Pension increases	(1 401)
5. Pensioner bonus	(2 445)
6. Pensioner mortality	3 660
7. Miscellaneous	1017
Surplus as at 30 June 2014	**69 752**

1 Interest on opening surplus

Interest on the opening surplus as at 30 June 2013 based on the assumed rate of interest in the previous statutory actuarial valuation, amounted to R30.018 million.

2. Change of basis

The valuation basis was strengthened to take account of changes to the investment strategy. The discount rate was increased from 7.79% p.a. to 9.04% p.a. The pension increase assumption was increased from 5.66% p.a. to 6.78% p.a. The net post retirement interest rate thus increased from 2.02% p.a. to 2.11% p.a.

The effect of change in the net post retirement interest rate was a strain of R7.403 million.

3. Investment returns

The return of 12.4% p.a. earned on the assets of the Pensions Account exceeded the return assumed in the previous valuation basis of 7.79% p.a. resulting in a surplus of R31.499 million.

4. Pension increase

The pension increase of 5.5% granted on 1 March 2014 exceeded the pension increases assumed in the previous valuation basis of 5.66% resulting in a strain of R1.401 million.

5. Pensioner bonus

The 100% of monthly pension bonus granted in December 2013 resulted in a strain of R2.445 million.

6. Pensioner mortality

Over the inter-valuation period there were more pensioner deaths than allowed for in the valuation basis. This resulted in a strain of R3.660 million.

7. Miscellaneous

Miscellaneous sources led to a net surplus of R1.017 million which is also the balancing item of the analysis.