Report for: INFORMATION

The Royal Borough Windsor & Maidenhead

Contains Confidential or Exempt Information	NO - Part I
Title	Pension Fund risks of delivering services differently
Responsible Officer(s)	Nick Greenwood, Pension Fund Manager
Contact officer, job title and phone number	Kevin Taylor Deputy Pension Fund Manager 01628 796715
Member reporting	N/A
For Consideration By	Berkshire Pension Fund and Pension Fund Advisory Panels
Date to be Considered	7 November 2016
Implementation Date if Not Called In	N/A
Affected Wards	N/A

REPORT SUMMARY

1. This report summarises the potential pension risks of scheme employers transferring the delivery of services to the private sector and the impact this could have on the Pension Fund.

If recommendations are adopted, how will residents, fund members and other stakeholders benefit?	
Benefits to residents and reasons why they will benefit	Dates by which residents can expect to notice a difference
1. These should contain actual benefits to residents. If there are none (for example an internal process) Please say so.	N/A

1. DETAILS OF RECOMMENDATIONS

RECOMMENDATION: That Panel notes this paper and attached documents at Appendix 1.

2. REASON FOR RECOMMENDATION(S) AND OPTIONS CONSIDERED

2.1 Where a scheme employer considers letting a service contract to an independent service provider the affected employees will normally transfer under a TUPE arrangement.

2.2 Whilst pensions are not covered by TUPE, best value authorities are required under the Best Value Staff Transfers (Pension Direction) 2007 to ensure that their transferring staff either have continued access to the LGPS through an admission agreement with the chosen independent service provider or to an alternative broadly comparable pension scheme as certified by the Government Actuary.

3 KEY IMPLICATIONS

3.1 Independent service providers upon admission to the Berkshire Pension Fund take on significant financial and administrative responsibilities. Whilst they will enter into a 'commercial contract' with the letting authority they will also enter into a three-way pension admission agreement between the letting authority, the service provider (as the new admission body) and the Royal Borough of Windsor & Maidenhead as the administering authority to the Berkshire Pension Fund.

3.2 As part of the service tender process, the letting authority is required to provide details of the pension costs associated with becoming an admission body to the Pension Fund. The Fund's actuary will produce a report for inclusion with the tender documentation which sets out the employer contribution rate required from the successful bidder upon becoming an admission body along with details of a bond or indemnity required to protect the Pension Fund against costs arising as a result of the admission agreement (service contract) terminating early. This will include underfunding (pension deficit), early retirement strain costs and unpaid contributions and other expenses associated with the premature termination of the admission agreement.

3.3 At the point the service contract comes to an end, or earlier if the last contributing scheme member leaves employment, the admission agreement will terminate and the actuary is required under the LGPS regulations to undertake a cessation valuation. This may, and is likely to, identify an exit payment payable by the admission body to the Pension Fund in order to pay for any deficit that has built up whilst the employer has been an admission body to the Fund.

3.4 It is important to note that when a group of employees TUPE transfer to a new employer that becomes an admission body to the Pension Fund, that new admission body is deemed to join the Fund as if it is 100% funded i.e. any deficit (or surplus) built up in the Pension Fund in respect of the transferring employees remains with the letting authority and does not pass to the new admission body.

3.5 However, any increase in that past service deficit during the lifetime of the service contract is met by the new admission body along with the future pension membership costs associated with those scheme members post-transfer of their employment.

3.6 Requirements set out under the LGPS regulations make it very clear what the responsibilities are of an admission body upon joining, and leaving, the Pension

Fund. These requirements are set out in the tripartite admission agreement completed at the start of the service contract. Most key to this is that the admission body will:

3.6.1 Pay the employer contributions at the rate certified by the Fund's actuary (as may be adjusted every three years as part of the triennial valuation exercise);

3.6.2 Arrange for a bond to the value set by the Fund's actuary to be in place throughout the contract period and as may be re-assessed by the actuary at any time (or alternatively provide a guarantor acceptable to the Pension Fund) ;

3.6.3 Make payment to the Pension Fund of any other additional costs identified throughout the period of the service contract; and

3.6.4 Make payment of any exit charge to the Pension Fund as assessed by the Fund's actuary at the termination of the admission agreement.

3.7 The costs identified in paragraph 3.6 can be considerable and will impact on a bidder's decision to apply for the service contract. When issuing their tender documentation the letting authority may choose to include details as to how they will deal with the issue of pension costs as part of their contract negotiations.

3.8 A letting authority can, as part of the service contract and therefore outside of the pension admission agreement, agree to retain or share the pension liabilities as identified by the actuary by an adjustment to the contract price. The letting authority could choose to pass all or none of the liabilities onto their chosen service provider or to come to an agreement to share those liabilities either though a 'pass-through' or a 'cap and collar' arrangement.

3.9 There are many ways in which an admission body may look to mitigate or limit exposure to the risks its participation in the LGPS will bring. It is for the letting authority to consider the level at which it feels comfortable in either retaining those risks or passing them onto the admission body.

4. FINANCIAL DETAILS

4.1 The financial risks to both the letting authority and the admission body can be considerable and are somewhat unquantifiable as the funding position of the admission body, and the Pension Fund as a whole, cannot be guaranteed as economic conditions change and investment returns vary over time.

4.2 There is a tendency at present for letting authorities to consider and agree to a full pass-through of liabilities. What this means is that an agreed rate of employer pension contribution is set between the letting authority and their chosen service provider as part of their service contract negotiations with any certified adjustments to the employer contribution rate being met by a variance in the contract price throughout the lifetime of the service contract.

4.3 Furthermore, there is currently an intention on behalf of the letting authority to retain all past and future pension liabilities and to agree to meet any deficit when the admission agreement comes to an end, whether or not that is commensurate with the termination of the service contract.

4.4 Recent experience shows that letting authorities are inclined to ignore the need for a bond/indemnity to be entered into or to at least restrict the value at which their chosen service provider will be expected to fund that bond.

4.5 In short, there is a recent trend for letting authorities to retain all of the pension risk and not to share or pass on any of the risk to the incoming admission body.

4.6 In addition, admission agreements tend to be closed. This means that only those individuals employed by the letting authority at the point of the service transfer retain the right to contribute to the LGPS whilst continuing to be employed in connection with service. No new employees appointed by the admission body can join the scheme.: Therefore:

4.6.1 The actual numbers of active scheme members diminish;
4.6.2 The actual amounts of employee and employer contributions paid to the Fund diminish;
4.6.3 The average age of the active members increases;
4.6.4 The numbers of deferred and pensioner members increases; and
4.6.5 The overall pension liabilities increase

4.7 The likely outcome of this situation is that the Pension Fund matures, the number of contributing members decreases, the number of deferred and pensioner members increases and scheme employers are required to pay increasing employer contributions and rising deficit recovery amounts.

5. LEGAL IMPLICATIONS

5.1 The Local Government Pension Scheme Regulations 2013 (as amended) set out the statutory provisions required of all scheme employers including admission bodies.

6. VALUE FOR MONEY

N/A

7. SUSTAINABILITY IMPACT APPRAISAL

N/A

8. RISK MANAGEMENT

8.1 The risks identified throughout this paper fall mainly on letting authorities where business decisions can have future implications for the funding of pension liabilities.

9. LINKS TO STRATEGIC OBJECTIVES

9.1 This paper links to the Borough’s current ‘delivering Services Differently’ policy.

10. EQUALITIES, HUMAN RIGHTS AND COMMUNITY COHESION

N/A

11. STAFFING/WORKFORCE AND ACCOMMODATION IMPLICATIONS

None.

12. PROPERTY AND ASSETS

None.

13. ANY OTHER IMPLICATIONS

None.

14. CONSULTATION

None.

15. TIMETABLE FOR IMPLEMENTATION

15.1 N/A

16. APPENDICES

- PLSA guides for employers participating in the LGPS
    - An Introduction to the LGPS for Scheduled Bodies;
    - Navigating Entry into the LGPS: For Local Government Contractors.

17. BACKGROUND INFORMATION

- The Local Government Pension Scheme Regulations 2013 (as amended) – Schedule 2, Part 3.