Appendix D

RECOMMENDATION FROM THE LBB PENSIONS TEAM FOR ALL NEW ADMITTED BODIES TO JOIN THE BARNET PENSION FUND ON A 'PASS THROUGH' BASIS

Introduction

1.1 The purpose of this paper is to set out the recommendation from the LBB Pensions Team ('the Pensions Team') that for all new admission bodies (i.e. new organisations that join the Fund, such as caterers), with an active membership of less than 100 people, are admitted to the London Borough of Barnet Pension Fund ('the Fund') on a 'pass-through' basis.

1.2 Pass-through is a way that admission bodies can participate in the Fund with certain risks being shared between the letting authority (i.e. the Council – including where contractors are employed by LEA schools, Middlesex University, Barnet & Southgate College and Academies) and the new contractor.

1.3 The Pensions Team have discussed the recommendation with both the Fund Actuary, Hymans Robertson, and the lawyers, Bevan Brittan.

Context

2.1 Under the Fund's current admissions policy for new contractors, the following principles apply:

- 2.1.1 all past service pension benefits in respect of outsourced members are transferred from the letting authority to the new contractor.
- 2.1.2 the contractor is set up on a "fully funded" basis using ongoing assumptions.
- 2.1.3 the starting contribution rate is the cost of future service benefits only.
- 2.1.4 the contribution rate is reviewed and adjusted at every formal valuation.
- 2.1.5 any early retirement strains and augmentation costs that arise are met by the contractor via an additional lump sum contribution.
- 2.1.6 a bond or other form of indemnity is taken out by the contractor.
- 2.1.7 on cessation, the resulting cessation valuation may lead to the payment of a cessation debt by the employer (or an exit credit by the Fund.)

2.2 Following cessation, the contractor makes a "clean break" from the Fund with no further obligations other than paying any cessation debt. The assets and liabilities left behind by the departing contractor revert to the letting authority (as required under the LGPS Regulations).

2.3 If the service is then contracted to another supplier then the assets and liabilities for the people who are employed under that contract are transferred to the new employer. As example of this is when ISS transferred services to Signature Education and people transferred their employment from ISS to Signature Education.

Appendix D

RECOMMENDATION FROM THE LBB PENSIONS TEAM FOR ALL NEW ADMITTED BODIES TO JOIN THE BARNET PENSION FUND ON A 'PASS THROUGH' BASIS

'Pass through' agreements

3.1 Under the current "traditional" approach to outsourcings (set out above), all the key pension risks transfer from the letting authority (e.g. the School) to the contractor for the duration of the contract (e.g. ISS).

3.2 For many contractors, this pension risk (which is often intangible in nature) may be viewed as an unexpected or undesirable by product, and this leads to additional administrative complexity for the Fund during the contractor's period of participation. In practice, pension considerations are often an afterthought in the commercial contract negotiations.

3.3 Similarly, the transfer of pension risks from Academies to contractors dilutes the effect of the Academies Guarantee provided by the Department of Education.

3.4 The traditional outsourcing approach leads to a great deal of uncertainty over costs for contractors because market conditions are uncertain e.g. large increases to regular contributions, big cessation debts etc. Bidders for contracts are increasingly aware of these problems and may seek to price them into contracts via additional service charges which can undermine the purpose of the outsourcing.

3.5 Under a pass-through arrangement the risks and cost volatility are passed back to the letting authority. This increases risk for the letting authority but simplifies the contractual situation with the contractor. Whilst a pass-through approach increases risk, in practice the letting authority will want to obtain the best price for the outsourced service. Offering contractors pass-through as a means for removing some of the uncertainty of the cost for paying for the outsourced member's pension benefits may be a way of helping to achieve this.

3.6 In addition, whether using the standard approach or pass-through, the letting authority still retains long term responsibility for the risks as all the members' accrued benefits transfer back to the letting authority at the end of the contract.

3.7 The letting authority also remains the ultimate guarantor for all pension obligations throughout the contract in the event of the contractor becoming insolvent. This is unchanged whether adopting the standard approach or using pass-through.

Appendix D

RECOMMENDATION FROM THE LBB PENSIONS TEAM FOR ALL NEW ADMITTED BODIES TO JOIN THE BARNET PENSION FUND ON A 'PASS THROUGH' BASIS

Benefits and risks of pass-through

Benefits of pass-through	**Risks of pass-through**
For the Letting Authority	**For the Letting Authority**
Letting authority may be able to negotiate better contract terms.	Assets and liabilities remain on accounting balance sheet.
Easier to understand their pension responsibilities.	Loss of a potential cessation debt at the end of contract.
Retains upside potential (i.e. retaining surpluses at end of contract).	Depending on design, the letting authority may be required to meet the cost of changes to LGPS benefits e.g. any strains relating to early retirements and augmentations.
Clearer and more consistent tendering process.	Mispricing the contract (eg if fixed rate was too low, in hindsight)
Avoids exit credits	
For the Contractor	**For the Contractor**
The contractor bears less pension risk.	Loss of a potential exit credit at the end of contract.
Greater certainty of contributions.	Potential for overpaying pension costs during the contract period.
No potential cessation debt to pay at the end of the contract.	
Reduced administrative costs as no requirement for a market risk bond.	
For the Administering Authority	**For the Administering Authority**
Ease of administration.	New documentation required, including maintenance of a clear policy on pass-through.
Reduction in time costs monitoring and administering bonds.	If implemented as a 'default' or 'optional' approach – the benefits may not be realised if letting authorities defer to traditional admissions approach.

Employer Statistics

4.1 As at the 31 March 2023, there were 70 employers in the Fund, of which 19 were admitted bodies (27%).

4.2 The average employer primary contribution rate for these admitted bodies is around 26% (the primary contribution rate for the Council is 19.1%).

Appendix D

RECOMMENDATION FROM THE LBB PENSIONS TEAM FOR ALL NEW ADMITTED BODIES TO JOIN THE BARNET PENSION FUND ON A 'PASS THROUGH' BASIS

4.3 In 2022/23, the total employer contributions paid was £44,900 million of which £2.25 million was paid by the admitted bodies (0.005%).

Current issues with the current Admissions process

5.1 The Pensions Team are usually informed at a relatively late stage that a new employer wants to apply for admitted body status, and this is usually after the admission has taken place (this increases risk for the Pension Team as we are legally exposed without having any legal agreement in place).

New Admitted Body	Date of Admission	Date Pensions Team notified of admission
Chequers Cleaning	01/12/2022	08/12/2022
Olive Dining (Holly Park School)	01/04/2023	26/04/2023
Olive Dining (Danegrove School)	01/05/2023	21/06/2023

5.2 Contracting is normally done by employer (typically schools) and the process involves the contractor joining the fund via an Admission Agreement (which is sealed).

5.3 Currently, the admission process can take months to complete. This is due to several factors, such as:

5.3.1 Determining the membership of the new admitted body, so data can be sent to the actuary to calculate the employer contribution rate.

5.3.2 Getting the admission agreement signed by the new admitted body, and in some cases, the letting authority. This can involve numerous chasers being sent and a lot of the time, it is the admitted body being unable to provide a bond that delays the agreement being signed.

5.3.3 The admission agreement are currently 'sealed' documents and delays have occurred with HB Law when the Pensions Team are trying to get the admission agreement sealed and finalised.

5.3.4 The issues with Signature Education and London Kosher Catering highlight the recent issues, the Pensions Team have had in getting admissions completed.

5.3.5 The contractor is also required to get a Bond and that process adds to the complexity. In theory, the Fund is protected from risks, but in practice the process is laborious and creates more risk particularly if contractors are unable or unwilling to provide a Bond. This is usually due to cost of obtaining the Bond, The Pension Fund does not have any direct way to enforce employers meet their requirements.

5.3.6 The reason for this is that in most new admissions, this involves between 3-5 staff being employed by the contractor earning relatively modest salaries of around £15k per annum and as such, it is difficult for the employer to obtain a Bond. The table below illustrates when recent new contractors joined the Fund and who have not yet provided a Bond.

Appendix D

RECOMMENDATION FROM THE LBB PENSIONS TEAM FOR ALL NEW ADMITTED BODIES TO JOIN THE BARNET PENSION FUND ON A 'PASS THROUGH' BASIS

Admitted Body	Date of Admission	Value of Bond
Innovate (St James)	01/08/2019	£81,000
Olive Dining (St Joseph's Primary)	01/08/2019	£50,000
Sancroft Community Care	01/06/2019	£101,000
Tenon (St Michaels)	01/04/2021	£8,000
Nourish Contract Catering Ltd (Osidge School)	01/08/2022	£2,000
CSSL	01/11/2002	tbc
Chequers Catering	01/12/2022	tbc
Olive Dining (Holly Park School)	01/04/2023	tbc
Olive Dining (Danegrove School)	01/05/2023	tbc

5.4 In most cases, the contractor does not start to pay both member and employer contributions over to the Fund until the admission agreement has been signed and sealed. However, the Pensions Team have started to ask new contractors to commence paying contributions to the Fund before this date, with the employer rate being set at 25%, with adjustments being made once the admission agreement is finalised.

5.5 The contractor will be liable to meet cost of any of their staff who are made redundant and pick up the cost of any ill health retirements.

5.6 The contractor is 'on risk' in that they pay a variable employer contribution rate and at the end of the contract they would be for deficit payable to the Fund, or they may be entitled to a return of some or all of the 'exit credit' (surplus). a refund. The last few cessations have all resulted in a surplus being potentially payable to the new employer.

Target Outcome

6.1 The LBB Pensions Team would like the recommendation for pass through to be the default arrangement for all new admissions with effect from 1 January 2024.

6.2 The default pass-through will apply to contracts let by all types of letting authority but will be limited to employers with under 100 active members.

RECOMMENDATION FROM THE LBB PENSIONS TEAM FOR ALL NEW ADMITTED BODIES TO JOIN THE BARNET PENSION FUND ON A 'PASS THROUGH' BASIS

6.3 The letting authority will retain all risks, with the exception of the award of additional pension/augmented benefits, and the award of unreduced early retirements (non ill-health).

6.4 The employer contribution rate may be different from the primary rate of the letting authority to reflect the higher risk to the letting authority from having a pass-through agreement. This is a commercial point which we would discuss with the letting authority. In practice though, if a higher pension cost is charged through the pass—through, the contractor will simply reflect this in their contract price and so the letting authority may wish to keep the contribution consistent with their own rate for simplicity. Another commercial consideration is whether the contractor updates the rate at each triennial valuation and how this gets shared with the contractors. It is worth noting that the Regional Enterprises pension agreement was effectively a pass-through with all changes in costs indemnified by the Council.

6.5 There will be no requirement for a bond to be arranged for default pass-through admissions. However, the Actuary will still calculate this figure so the letting authority understands the risks retained. Assets and liabilities will be retained by the letting authority during the period of participation.

6.6 For current admitted bodies, when either their contract renews or when their exiting bond expires, they will be considered on a case-by-case basis on whether the pass-through policy will apply to them going forward.

6.7 A current issue is the process for getting new Admission Agreements sealed is very time consuming. The Pensions Team is aware of market solutions which largely automate this process and as an extension to amending the approach to a pass-through, we will be bringing a business case which looks to implement an automated admission process. This will reduce risk significantly as timescales for finalising documents will be significantly shorter.

6.8 If we proceed with the recommendation the new Admissions policy will be updated to include this new process.

Recommendation

7.1 In terms of process, and subject to comments from the Section 151 Officer, we will look notify the Pension Fund Committee of the proposed change of approach at the 2 November 2023 Pension Fund Committee meeting and assuming no objections, we would look to implement a pass-through from 1 January 2024.

7.2 If the recommendation is agreed, the Pensions Team will update all employers as soon as possible after the new Admissions policy has been signed off.

Appendix D

RECOMMENDATION FROM THE LBB PENSIONS TEAM FOR ALL NEW ADMITTED BODIES TO JOIN THE BARNET PENSION FUND ON A 'PASS THROUGH' BASIS

7.3 The Local Pensions Board will also be updated on the changes to the new Admissions Policy.