Report for: Pensions Committee and Board 11 July 2019

Title: London Collective Investment Vehicle (CIV) – Pensions Recharge and Guarantee and Service Level Agreement (SLA)

Report authorised by: Jon Warlow, Director of Finance (S151 Officer)

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Ward(s) affected: N/A

Report for Key/ Non Key Decision: Non Key decision

1. Describe the issue under consideration

1.1. The purpose of the paper is to provide information to update members of the Pensions Committee and Board regarding the London CIV's pensions recharge and guarantee agreements, and the recently issued Service Level Agreement.

2. Cabinet Member Introduction

2.1. Not applicable.

3. Recommendations

3.1. The Committee and Board note the contents of this report, and any other verbal updates provided by officers and the fund's Independent Advisor in the meeting.

3.2. The Committee and Board approve both the pensions recharge and guarantee agreements attached at Appendices 2 & 3 and for these documents to be entered into, and give delegated authority to the Section 151 officer to approve any subsequent minor amendments to these two documents.

3.3. The Committee and Board approve the draft SLA to be entered into with the London CIV attached at Appendix 6 and give delegated authority to the section 151 Officer to agree the final SLA .

4. Reason for Decision

Guarantee

4.1. In order for the London CIV to be admitted to the City of London Pension Fund, the City requires some kind of indemnification, against future pension liabilities. When a new scheme employer body is admitted to an LGPS fund generally, it is normal for the fund to look to get a form of indemnification against the new scheme employer becoming insolvent or failing to pay across the employer contributions it should. This is usually done via a guarantee, or the new scheme employer producing a bond (essentially an insurance policy). Should an employer default, the fund can then call upon the bond (or guarantee) to make good any unpaid contributions or deficits due to it. A bond comes at a cost, which is then a revenue cost to the new employer. Initial work completed by the CIV has indicated that this kind of arrangement will not be economical or in either the CIV or boroughs best interests.

4.2. The CIV's revenue resources essentially originate from the London Borough pension funds, who pay fees to the CIV for managing assets, or development financing charges for the CIV's initial years of operation. If the City of London asked the CIV to provide a bond, the CIV would then have to set aside additional revenue resource (funded by the borough funds) to finance this bond.

4.3. At the time of the London CIV's set up, the issue of whether to offer LGPS pensions to CIV staff at all was debated. It was decided that it would be inappropriate for a quasi governmental organisation which has been set up for the LGPS to not offer LGPS pensions to its own staff. It was also anticipated at the time, that many of the staff members who would work for the CIV would come from LGPS funds, hence continuing to offer LGPS pensions would be a key factor in attracting staff.

4.4. The draft guarantee is set out at confidential appendix 2, alongside the CIV's remuneration policy and LGPS discretions policies at confidential appendices 4 &5, and a question and answer at Confidential Appendix 1 which provides further information about both the guarantee and recharge.

Recharging Agreement

4.5. The CIV has to abide by FCA regulations about the value of capital it holds on its balance sheet relative to liabilities, i.e. if their pensions deficit increases, the CIV will have to hold additional assets to be FCA compliant. In practice, were this to occur, the CIV would have to essentially charge the boroughs additional fees to generate this capital so that they could hold additional assets to offset the pension liability.

4.6. Executing the recharging agreement allows the CIV to recognise an asset on their balance sheet for accounting purposes of equal and opposite magnitude to their pension liability (if one should exist), at any point in time, thus negating the requirement for them to hold any additional capital to offset their pensions liability.

4.7. The draft recharging agreement is set out at confidential appendix 3.

<u>Service Level Agreement (SLA)</u>

4.8. The CIV has provided a draft SLA to London Boroughs, to formalise the interactions between boroughs and the CIV, as a provider of services to Boroughs. It sets out various details of how the CIV and Boroughs will interact. The draft SLA is set out at Confidential Appendix 6.

5. Other options considered

5.1. None

6. Background information

<u>Guarantee</u>

6.1. The Government has made asset pooling mandatory for all Local Government Pension Schemes, and eight 'pools' have been set up nationally for this purpose with all LGPS Funds belonging to one pool. The London Collective Investment Vehicle (CIV) is the pool for the 31 London Funds and the City of London, (formerly 32 funds prior to the Richmond and Wandsworth fund merger).

6.2. When the London CIV was formed by the London Boroughs, offering LGPS pension rights to CIV staff was felt to be appropriate given that the CIV is quasi governmental and is set up for the purpose of investing LGPS assets. It was also felt to be a significant recruitment tool which might attract current LGPS officers to consider working for the CIV. In order to provide LGPS pensions, the CIV had to become an admitted body to one of the Funds – this was done with the City of London Fund. The boroughs agreed to jointly act as guarantors to the City of London Fund, so that any future liabilities would be shared jointly and equally between the funds.

6.3. The guarantee agreement has been drafted so that, in the event that London CIV's admission agreement with the Fund terminates (or if it otherwise ceases to have any active members left in the Fund) and the company fails to pay any exit payment due under Regulation 64(2) of the LGPS 2013 Regulations, each of the Shareholders will, on a several basis, pay their 'proportionate share' of the unpaid exit payment. The proportionate share is based on the number of shareholder authorities listed in the schedule to the agreement and based on the current number of shareholders is 1/32nd each. This reflects the transfer of Richmond's shares in London CIV to Wandsworth pursuant to The Local Government Pension Scheme (Wandsworth and Richmond Fund) Regulations 2016 (SI 2016/1241).

Recharge Agreement

6.4. The recharge agreement provides a mechanism for the shareholders to reimburse London CIV (not the Fund) for the pension costs the company has to pay to the Fund, including its regular monthly employer contributions due under its rates and adjustment certificate, any one-off contributions such as strain costs payable on redundancy or ill health early retirement and any exit payment arising on termination of the admission agreement (or if London CIV otherwise ceases to have any active members left in the Fund).

6.5. The purpose of this agreement is to create an ‘asset’ on the company’s balance sheet which can be used to counter any balance sheet liability representing any deficit in the Fund (as calculated on an accounting basis) resulting from the company’s participation in the Fund as an admission body.

6.6. London CIV’s annual financial statements are prepared in accordance with Financial Reporting Standard 102. In applying the general recognition principle in paragraph 28.3 of the Standard to defined benefit pension plans such as the LGPS, London CIV has to recognise a liability for its obligations in the Fund net of its share of Fund assets. For this purpose, liabilities are calculated on a different actuarial basis to the basis actually used by the Fund’s actuary to carry out Fund valuations. This calculation may result in a deficit liability on London CIV’s balance sheet. This could in turn affect level of regulatory capital that the company needs to hold to satisfy the FCA.

6.7. However, under paragraph 28.28 of Financial Reporting Standard 102, if London CIV is virtually certain that another party or parties will reimburse some or all of the expenditure required to settle a defined benefit obligation then the company can recognise its right to that reimbursement as a separate asset in its annual financial statements and shall treat that asset in the same way as its share of the Fund assets. The recharge agreement is intended to act as such an asset.

7. Contribution to Strategic Outcomes

7.1. Not applicable

8. Statutory Officers comments (Chief Finance Officer (including procurement), Assistant Director of Corporate Governance, Equalities)

Finance and Procurement

8.1. There are no direct immediate financial implications arising from this report. Haringey, along with all other London Boroughs and the City of London, is an equal shareholder in the London CIV, the recharging and guarantees formalise the existing pensions arrangements with the London CIV. The costs associated with the operation and management of the London CIV, are all legitimate pension costs which should be included within the costs of operation of Haringey Pension Fund.

Legal Services Comments

8.2. The Council as administering authority for the Fund is a member of the London LGPS CIV Limited (“CIV”). The CIV is entering into an Admission Agreement with the Administering Authority (the City of London Corporation). The Recharge Agreement will create a legal obligation on the Council to reimburse the CIV a proportion of its pension costs paid to the Administering Authority (the City of London Corporation). In addition, the Council will also be providing a guarantee to the Administering Authority in respect of any deficits in the fund should the CIV default from its obligations under the Admission Agreement.

8.3. The Service Level Agreement will be entered into between the CIV and each of its members. This agreement sets out the framework by which the CIV will deliver its services to the members, including quality standards, in order that the members can deliver their pooling plans.

Equalities

8.4. None applicable.

9. Use of Appendices

9.1. Confidential Appendix 1: Recharge and Guarantee Q&A
9.2. Confidential Appendix 2: DRAFT Guarantee
9.3. Confidential Appendix 3: DRAFT Recharge
9.4. Confidential Appendix 4: LCIV Discretionary policies
9.5. Confidential Appendix 5: Remuneration Policy
9.6. Confidential Appendix 6: LCIV DRAFT Service Level Agreement

10. Local Government (Access to Information) Act 1985

10.1. Not applicable.