Havering
LONDON BOROUGH

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| # CABINET | **13 November 2018** |
| **Subject Heading:** | **Havering Colleges Proposed Merger – Local Government Pension Scheme (LGPS) considerations** |
| **Cabinet Member:** | Cabinet Member for Finance and Property, Councillor Roger Ramsey |
| **SLT Lead:** | Chief Operating Officer – Jane West |
| **Report Author and contact details:** | **Debbie Ford**<br>**01708432569**<br>**Debbie.ford@onesource.co.uk** |
| **Policy context:** | **Havering Colleges restructuring and merger and Local Government Pension Scheme (LGPS) considerations** |
| **Financial summary:** | **Potential cash transfer to London Pensions Fund Authority as calculated and agreed with Actuaries.** |
| **Is this a Key Decision?** | • **YES – because;**<br>• **£500,000(or more from Pension Fund)**<br>• **Significant effect on two or more Wards** |
| **When should this matter be reviewed?** | **.In the spring of 2019 following feedback from the Secretary of State.** |
| **Reviewing OSC:** | **The Overview and Scrutiny Board will be responsible for reviewing the decision if called-in or once implemented** |

## The subject matter of this report deals with the following Council Objectives

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| Communities making Havering | [X] |
| Places making Havering | [X] |
| Opportunities making Havering | [X] |
| Connections making Havering | [X] |

## SUMMARY

**Havering Sixth Form College ("HSFC") and Havering College of Further & Higher Education ("HCFHE") are considering a merger with New City College ("NCC").**

**The pensions of the HSFC and the HCFHE staff who are members of the Local Government Pension Scheme may transfer on merger. This report outlines the potential material, substantial financial risks to the Council's Pension Fund in relation to the options Cabinet are being asked to consider.**

## RECOMMENDATIONS

**That Cabinet:**

1. **Considers  the Funds Actuary report at Appendix A (exempt)**
2. **Notes the summary of initial legal advice as the rider to Appendix A (confidential and exempt).**
3. **Considers the comments from HCFHE on the rationale for the merger of HCFHE and HSFC with NCC at Appendix B (exempt)**
4. **Agrees the College's request to transfer all HCFHE and HSFC members from the Havering Pension Fund to the London Pensions Fund Authority (LPFA) as set out in Option A in this report.**
5. **Delegates authority to Chief Operating Officer to take all necessary actions and steps she considers appropriate in order to give effect to this decision.**

## REPORT DETAIL

**BACKGROUND:**

1. As a consequence of an increasing number of colleges experiencing financial challenges, the government commenced a national programme of area based reviews covering further education and sixth form colleges in 2016, the intention of which is to create fewer, more effective and more sustainable colleges

2. A number of financial economic challenges facing the colleges are the main driver for a proposed merger. An earlier attempt for HCFHE to merge with Barking and Dagenham did not go ahead. The current proposal is for both the HCFHE and HSFC to merge with NCC.

3. NCC was created by the merger of Hackney Community College and Tower Hamlets College in 2016, Redbridge College in 2017 and Epping Forest in August 2018. NCC Pensions Administering Authority is the London Pensions Fund Authority (LPFA).

4. In preparation for the merger the colleges have requested permission from Havering as the Administering Authority to transfer the pension arrangements for all staff of the colleges (current and former employees) from the Havering Pension Fund to the LPFA.

5. HCFHE has produced a paper setting out the rationale for the merger for members to consider and this is attached as Appendix B.

6. The Fund's Actuary (Hymans) has produced a report, attached as Appendix A, and sets out the possible two scenarios of the proposed mergers to be considered

   a. Scenario A - where all members (actives, deferred and pensioners) transfer out to LPFA.

   b. Scenario B – where only active members transfer their past service out to LPFA.

7. Secretary of State Approval would be needed to transfer the pension rights of former employees from one LGPS Fund to another under scenario A. Once permission has been granted by Havering then the colleges will proceed with seeking Secretary of State approval

8. The Secretary of State will consult with all parties (all three colleges and both Funds) before granting approval. However, if all parties are agreeable, Secretary of State Approval is likely to be granted. The approval process takes about 2 – 3 months to process.

9. No approval is required from the Secretary of State if only current employees transfer over under scenario B.

10. Both colleges have confirmed that given their existing and future economic financial pressures they would not be able to proceed with the merger unless all members transferred out to the LPFA under scenario A.

11. Because of the complexity and the nature of the proposals involving the pensions of the Havering staff involved, initial external legal advice has been taken, confirming the points above. A summary of this is a rider to Appendix A. The appropriate law firm, Bevan Brittan gave this advice, on the basis the information set out in this Report and further, confirmatory advice will be obtained as needed prior to any major steps being taken.

## REASONS AND OPTIONS

### Options

1. **Scenario A - where all members (actives, deferred and pensioners) transfer out to LPFA.**

    a. The Pension Fund will be required to transfer assets and liabilities over to the LPFA to fund the transfer move as calculated and agreed by both actuaries for the Havering scheme and the LPFA scheme.

    b. This value of the transfer will be funded from a sell down of assets and this will have implications for the Pension Fund Investment Strategy. However, the current strategy includes target allocations across different asset classes that the Fund is working to meet. As the full investment in some of these asset classes take a number of years to be fully invested it is not anticipated that having to use the sale of assets to fund the transfer instead of the new mandates will be to the detriment of the strategy.

    c. Whilst the Colleges are planning for a merger date of no later than April 2019 any monetary transfers are likely to take place during 2019/20. The Pensions Committee will be presented with a report at a later date once the merger progresses for confirmation as to how to fund the transfer.

    d. The value of the Assets and liabilities will be reduced and result in an overall reduction in the Funding level of c0.8%, down from 69.7% to 68.9%.

    e. In addition to the Fund having to sell assets to pay the LPFA it will also lose the positive cash flow position from the colleges. This will put pressure on the cash flow over the longer term. The Fund currently reinvests investment income (i.e. dividends and interest) where possible but the fund can switch to draw down this income to maintain minimum cash thresholds, this could potentially impact investment growth.

f. The Investment Strategy will also need to give consideration over the longer term as to how to address any potential cash flow problems by utilising mandates that can provide the necessary cash flow. Over the next few years the Fund will receive income distribution from the Real Assets and Private Debt mandates that may mitigate the need to use dividend and interest income. The Pensions Committee will be asked to review the cash management policy once the cash requirements have been identified.

**2. Scenario B – where only actives members transfer past service transfer out to LPFA.**

a. If only Active members transfer out, as permitted under TUPE regulations, the deferred and pensioners would remain in the Fund.

b. The Actuary has provisionally calculated the share of assets assigned to the colleges and deducted from this share the amount the Fund would need to retain to cover the past service liabilities for the deferred and pensioners remaining in the Fund. The remaining amount of asset value would transfer to LPFA to fund the transferring active liabilities.

c. The size of the asset valuation required to pay the LPFA could be funded through current cash levels and would not require a sell down of asset.

d. The asset share is not enough to cover the liabilities of the transferring active members and would therefore require a significant ‘top up’ payment that the colleges would be required to pay over to the LPFA.

e. Given the size of the ‘top up’ payment both colleges have confirmed that given their existing and future economic financial pressures they would not be able to proceed with the merger under scenario B.

f. Whilst any merger under scenario B would not require a sell down of assets it would leave the fund with no employer contribution income to support pension benefits being paid out in the future. This would consequently increase pressure on the cash flow over the longer term and as with scenario A, the Committee will be asked to review the cash management policy once the value of any cash requirements have been identified.

g. When the last active member leaves the Fund this triggers a cessation payment. In this instance no cessation payment from the colleges would be required to the fund due to their calculated asset share exceeding their liabilities.

h. There would be a slight improvement to the funding level post transfer increasing to 70.7% from 69.7%.

i. **To support the future of the colleges, it is recommended that the Cabinet agree to the transfer of all members as detailed under scenario A, as outlined above to allow the merger of the colleges to proceed.**

## 3. Other options considered:

a. Given the size of the ‘top up’ payment both colleges have confirmed that given their existing and future economic financial pressures they would not be able to proceed with the merger under scenario B. For this reason scenario B is recommended to be rejected.

b. The Hymans report also mentioned that there may be a scenario where a transfer would not be necessary (i.e. where New City would be admitted to Havering in respect of former HSFC and HCFHE staff). Given that the approach adopted by NCC with previous mergers is to consolidate all LGPS arrangements into the LPFA scheme, for reasons of economies of scale, funding strength to absorb new members and easier for NCC to administer just one LGPS scheme, the option to transfer to the Havering scheme was not considered. NCC have confirmed that moving the whole of the NCC membership to the Havering Pension Fund is not this an option they would consider.

## IMPLICATIONS AND RISKS

### Financial implications and risks:

Financial implications are set out in Hymans report attached as Appendix A. and the effect on the Havering Pension fund is as outlined above.

These financial implications are indicative and based on market conditions as at June 18 and will be subject to final figures settled at transfer date.

Whilst the Colleges are planning for a merger date of no later than April 2019 any monetary transfers are likely to take place during 2019/20. The Pensions Committee will be presented with a report at a later date once the merger progresses for confirmation as to how to fund the transfer.

Any costs associated with the transfer will be met by the Colleges

The Pensions Committee were presented with a report for noting at the Pensions Committee meeting on the 18 September 2018 so members are aware of the future decisions they will need to make with regard to financing the transfer and reviewing the cash management policy.

Whilst there is a risk that future investment growth may impact the General Fund through the employer contribution rates it is not expected that this transfer in it entirety would be a material contributory factor.

**Legal implications and risks:**

This report has the benefit of specialist legal advice from the council's law firm Bevan Brittan.  This is the initial advice based on this report and will be supplemented as needed in due course.

The summary of the advice is in the Rider at the end of Appendix A. The legal advice confirms that the steps proposed are legally permissible. Ongoing legal advice will be provided to enable this arrangement to come to fruition.

**Human Resources implications and risks:**

Scenario A - where all members (actives, deferred and pensioners) transfer out to LPFA. – under this scenario existing access to the LGPS will be maintained for all existing members but there will a change to the pension arrangements and the Administrating Authority will change from Havering Council to the LPFA.

Scenario B – where only actives members transfer past service transfer out to LPFA.

If only Active members transfer out, as permitted under TUPE regulations, then TUPE protections will apply to ensure continued access to the LGPS. There would be a change to the Administering Authority as with under scenario A but for the deferred and pensioners remaining then membership would continue to be administered by Havering Council.

**Equalities implications and risks:**

The Public Sector Equality Duty (PSED) under section 149 of the Equality Act 2010 requires the Council, when exercising its functions, to have due regard to:

i. the need to eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010;
ii. the need to advance equality of opportunity between persons who share protected characteristics and those who do not, and;

iii. foster good relations between those who have protected characteristics and those who do not.

Note: ‘Protected characteristics’ are: age, sex, race, disability, sexual orientation, marriage and civil partnerships, religion or belief, pregnancy and maternity and gender reassignment/identity.

The Council is committed to all of the above in the provision, procurement and commissioning of its services, and the employment of its workforce. In addition, the Council is also committed to improving the quality of life and wellbeing for all Havering residents in respect of socio-economics and health determinants

## BACKGROUND PAPERS