QUANTUM ADVISORY
WORKING IN PARTNERSHIP WITH YOU

# Pension Opportunities for Housing Associations

We have been living in unprecedented times. COVID-19 and the war in Ukraine has shaken the world and its financial markets. High inflation, high borrowing costs and a poor economic outlook are the current problems for Governments to solve and the resulting fallout for pension schemes needs to be carefully considered and managed by employers.

Many Housing Associations participate in either the Local Government Pension Scheme (LGPS) or the Social Housing Pension Scheme (SHPS). As a Housing Association employer of a defined benefit multi-employer pension scheme, what issues are you seeing?

In our experience we are seeing Housing Association's considering the following issues:

- *LGPS valuation results and new pension contributions coming in force from 1 April 2023 and what does it mean for their business.*
- *Housing Associations looking at their options on exiting the LGPS.*
- *Preparing for big changes in pension accounting positions.*
- *SHPS benefit review and the consequence for Housing Associations.*
- *What the improvements in the SHPS funding level mean for future SHPS contributions.*

## LGPS valuation results and pension contributions changing from 1 April 2023

Housing Associations that participate in the LGPS have recently received their 1 April 2022 LGPS valuation results and depending on the LGPS Fund they participate in and their own circumstances, for many, contribution requirements will be broadly neutral compared to what is currently being paid. Results of the calculations are highly correlated to the expected future real returns on the LGPS Fund's portfolio of assets and whilst this probably will have worsened since the last contribution assessment for past service benefits this is likely to have been offset, and more, by the impressive returns actually experienced on LGPS Fund portfolios meaning that past service deficits may have reduced, or surpluses increased.

As a result, we have seen secondary contributions, which are used to recoup deficits over a period have generally reduced for Associations that remain in a deficit position. However primary contributions, which cover the cost of future accrual for active members are not impacted by actual investment returns so commonly we have seen these increase.

*"Generally speaking employers with a large proportion of contributing members are likely to have seen some increase in contributions unless they are very well funded. Employers with fewer contributors, perhaps those using DC schemes for new joiners, are likely to have fared better"*

## Employers exiting the LGPS

The risk and cost of LGPS membership isn't for all Housing Associations. Usually Housing Associations have a range of options when it comes to pension provision for their employees. The most common alternative to the LGPS being the lower cost and low risk defined contribution (DC) option. Many Housing Associations have been considering exiting the LGPS over recent years, wanting to pass their obligations back to the LGPS Fund and completely remove all the related risks and liabilities from their balance sheet with all employees in a DC arrangement for future service. Usually, the cost of exiting the LGPS has been a big obstacle stopping them from doing this.

> *"For employers that have planned to exit the LGPS but found the associated exit costs unaffordable, the recent repricing in the bond and gilt markets is a game changer. We expect many employers will find this option much more affordable now than when they last considered it"*

Unlike the employer contribution reassessment calculation, exit cost calculations are usually carried out on a 'minimum risk basis' and gilts are usually a heavy component of this. Whilst LGPS Funds and their actuaries have discretion in the way their minimum risk basis is constructed, the sharp increases in gilt yields seen over 2022 have translated into exit valuations that are much more affordable than we have seen historically. This presents an interesting opportunity for many employers. We therefore expect many to approach their LGPS Fund seeking exit whilst the environment is favourable.

As a crude indication, looking at the movement in gilt yields and inflation expectations, an employer may find that the value of their pension obligations on an exit basis today has reduced by 1/3rd or so compared to three years earlier.

> *"That means an employer with £30m in liabilities and an exit deficit of £10m may now find themselves fully funded and could exit the LGPS for free"*

This is the sort of improvement we are seeing first hand in employer LGPS exit costs.

Those Housing Associations who cannot or do not wish to exit, perhaps because they want to retain active contributors in the LGPS or the exit cost remains unaffordable also have options. The concept of 'de-risking' in the LGPS universe might be relatively new but employer appetite for it is not and the sharp rise in gilt yields has led to many Housing Associations discussing their options with their LGPS Fund.

## Housing Association accounting positions

Whilst high inflation and the sharp increase in gilt yields have stolen the headlines for a variety of reasons, corporate bond yields have risen sharply too. Meanwhile long-term inflation expectations have reduced.

> *"All Housing Associations' accounting positions must be calculated using corporate bond yields so if employers with a 31 March 2022 year-end reassessed the position today, they would see significant improvements"*

Asset values may have fallen slightly over the last 12 months, but this is unlikely to have offset much of these gains. We haven't quite reached 31 March 2023 but the signs so far this financial year are encouraging and we expect some very positive swings in Housing Association's balance sheets, which may cause its own problems.

## SHPS benefit review and pension increase issue

Following a benefit review by the SHPS trustees there is uncertainty about how some SHPS benefits should increase in payment. The SHPS trustees, are asking the Court to provide clarity on the issue. The potential consequence is that some members' benefits may not have increased correctly to date (too low) and correcting this will result in additional liability for all participating employers. The estimated additional liability is expected to be in the region of 4% of SHPS liabilities which equates to around £150m. Exactly how this will impact each employer will differ.

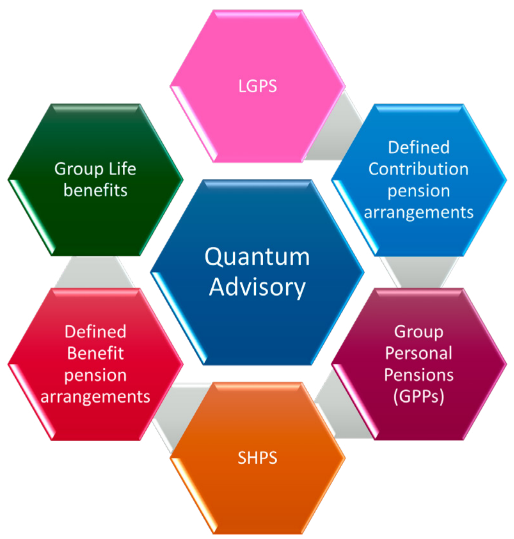
> *"Employers would not be expected to pay any additional liability as a one-off lump sum. Instead it would be loaded to each employer's SHPS liabilities at a future valuation so would be met as part of the regular deficit contributions paid to SHPS i.e. the additional liability will be paid off over a period of time"*

## Improvement in SHPS funding position

Since the 30 September 2020 funding valuation, changes in financial conditions have meant that the SHPS deficit has halved from c£1.5bn to c£0.75bn. If there are no significant changes between now and the next funding valuation in September this year it is likely that new contribution rates that would come into force from April 2025 in respect of the SHPS deficit and future service will reduce compared to what is being paid now.

> *"At last, employers' contributions to SHPS are likely to reduce from April 2025 after continual increases over the last 10 to 15 years. This will be good news especially for those Housing Associations who have kept the SHPS defined benefit scheme open to accrual for their employees*

## We have expertise in:



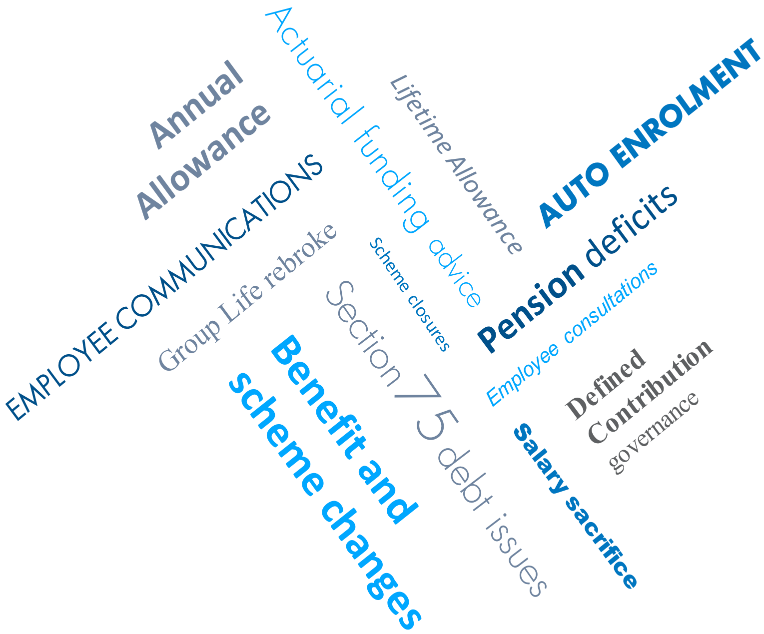
## Quantum Advisory Multi-Employer & Public Sector pension team

If you would like to discuss any of the content above in more detail then please feel free to contact us directly.  We have much experience in assisting Housing Associations with their pension and employee benefit requirements.


**Stuart Price, Partner & Actuary**
Cypress House
Pascal Close, St Mellons
Cardiff CF3 0LW
stuart.price@qallp.co.uk

**Adam Cottrell, Senior Consultant & Actuary**
Cypress House
Pascal Close, St Mellons
Cardiff CF3 0LW
adam.cottrell@qallp.co.uk


## We can help with:




## Quantum Advisory

Established in 2000, Quantum Advisory is an independent financial services consultancy that provides solution based pensions and employee benefit services to employers, scheme trustees and members. We design, maintain and review pension schemes and related employee benefits so that they operate efficiently and effectively and are valued by employees. This means that you can get on with doing the things that you do best, therefore saving you time and money

Quantum has offices in Amersham, Birmingham, Cardiff and London. Get in touch to see how we can help with your risk transfer, pension and employee benefit challenges.



QUANTUM ADVISORY
WORKING IN PARTNERSHIP WITH YOU
www.quantumadvisory.co.uk