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Housing briefing, October 2020
LGPS – Do you have to exit through the gift shop?

In our August briefing, we outlined new flexibilities offering housing associations an alternative exit route out of the LGPS.

With new legislation in place, this briefing considers the potential options available when planning to end benefit accrual. Is this a chance to exit via a conveniently open side-door rather than through the expensive gift shop?

Finally, we are speaking at the Just Housing Conference 2020 organised by Brabners LLP. Registration details are shown at the end of this briefing.

Stuck between a rock and a hard place

Up until now, many housing associations with LGPS obligations have been stuck between a rock and a hard place – expensive to stay, expensive to leave.

A popular (interim) measure is to close the LGPS to new entrants so the issue is kicked down the road. But the road to the end game will start, and funds often increase employer contributions as a closed (ageing) membership is more expensive than a younger membership with time on its side.

However, when primary rates (or 'future service' rates in elsewhere in planet pensions) can be anywhere between 15% and 40% it becomes harder and harder for boards to stand by and watch pension costs between different parts of the workforce diverge to such a large degree.

Then there's the secondary contributions (or 'deficit payments' elsewhere in planet pensions) which seem to go up even when there's a funding surplus…

"100% funded" they said, following a large scale voluntary transfer. But 100% funded in one universe, is not 100% funded in another: 100% funded on a cessation basis in 2020 is a very different universe to 100% funded on an ongoing basis in 2000.

Following a consultation last year, we now have two useful new options created in the LGPS regulations with effect from 23 September 2020.

New exit strategies, but to stick or twist?

Stick – spread exit payments

Whilst the ability to spread exit payments has been a flexibility in some regional funds' policies for a good while, this new overarching legislation is very welcome.

As a general rule, we welcome long-term thinking and time can often be our friend when it comes to managing pension scheme obligations.

If you agree to spread the payments the exit debt becomes a "fixed liability". However, in most cases keeping the exit debt a "floating liability" is expected to cost less in the medium term.

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Having the ability to retain the growth-potential of the fund assets to offset some of the cash payments to settle a crystallised debt is an interesting concept to consider and model.

Or twist – deferred debt arrangements

How about being able to stop paying primary contributions (well, replace them with the cost of an alternative scheme) and continue to pay secondary contributions without crystallising the debt? This can be attractive if you understand the risk.

Crystallising an exit debt on negative yielding gilts has never made much sense to us. Staying 'on the hook' for deficit payments on the ongoing funding basis with a return-seeking investment strategy sounds much more palatable.

Stick or twist? Risk or opportunity?

Risk is a funny word. It gets bandied around with mostly negative connotations. But what is riskier – crystallising a debt assuming that the assets held lose money, or allowing return-seeking assets to seek returns and offset cash payments? Our recommendation is to compare the "stick" and "twist" options with a variety of scenario testing and stochastic modelling of the possible costs to help our clients decide which is the most suitable option for them.

Over to the funds…

Whilst we've had legislative change, now it's over to the regional funds to update their Funding Strategy Statements with policies on spreading exit payments and introducing deferred debt arrangements.

Please keep an eye out for your LGPS consulting on changes to its funding policies, and speak to us if you'd like hear our view on what your fund is proposing.

The £95,000 public service exit cap

Coming into force on 4 November 2020 is the long-mooted cap on public sector exit payments.

Whilst we won't go into all the payments which are covered by the cap here, pensions-wise a 'strain cost' will be included which can have a significant impact on both LGPS members and LGPS employers – particularly where employees are made redundant, or who leave employment for business efficiency reasons, on or after age 55.

But, and this is a big but, are housing associations exempt from these regulations? Well, housing associations are not included in the list of 'capped employers' but this may not be as black and white as it may seem as there may be some contractual issues to consider – legal advice would be highly recommended.

CDC moves a step closer

Collective Defined Contribution (CDC) schemes moved a step closer this month as the Pensions Schemes Bill moved to committee stage. Our briefing in June 2018 introduced the key features of CDC. We know many large associations are considering CDC and now is the ideal time to schedule some training for your board or relevant committee. Please contact us if this training is of interest.

Just Housing Conference 2020

Finally, we are delighted to have been invited to speak at Brabners' conference specifically designed for housing associations. You can register at:

https://events.brabners.com/just-housing-conference-2020

How First Actuarial can help you

First Actuarial provides independent advice to more housing associations than any other firm.

If you would like to discuss pensions with us, then please contact your usual First Actuarial consultant or any of our nationwide housing specialists.

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