Housing briefing, June 2022
Has SHPS been paying the correct benefits?

The Trustee of the Social Housing Pension Scheme (SHPS) is going to court to ask them to rule whether they have been paying the correct benefits to members. This means uncertainty for members and potential additional liabilities for employers to fund.

Background

In a recent communication, TPT confirmed that there is some uncertainty about the benefits that have been paid to members of SHPS, and that the Trustee has received legal advice that it should ask the court to provide clarity.

Following an earlier communication with employers, in 2021, TPT has identified a further "*potentially significant item*" relating to the pension increases in payment applied to benefits earned before December 2003. The total potential additional liabilities arising from all issues now identified have been estimated at **£233m** (around 3.9% of the total liabilities).

This figure is an average for SHPS as a whole. The impact on individual employers ***will*** vary, as each employer will have different proportions of benefits earned before and after December 2003. Employers with a larger proportion of pre-2003 service are likely to see a larger increase, and vice versa. Employers will understandably be disappointed with this news.

In this briefing we explain:

- The reason for the potential increase in liabilities
- The impact on members
- The funding and accounting impact on employers
- Next steps that employers should be considering.

Explanation of the main issue

The majority of the potential increase in liabilities (£150m out of £233m) arises from uncertainty about what pension increases should be applied to benefits earned by members before December 2003 (pre-2003 benefits).

Before 2011, the pension increases applied to pre-2003 benefits were in line with RPI inflation (capped at 5% pa). In 2011, TPT changed its approach and applied increases with a different measure (CPI inflation).

The court is being asked to consider whether pre-2003 benefits should have continued to receive pension increases in line with RPI inflation, rather than being switched to CPI inflation from 2011 onwards.

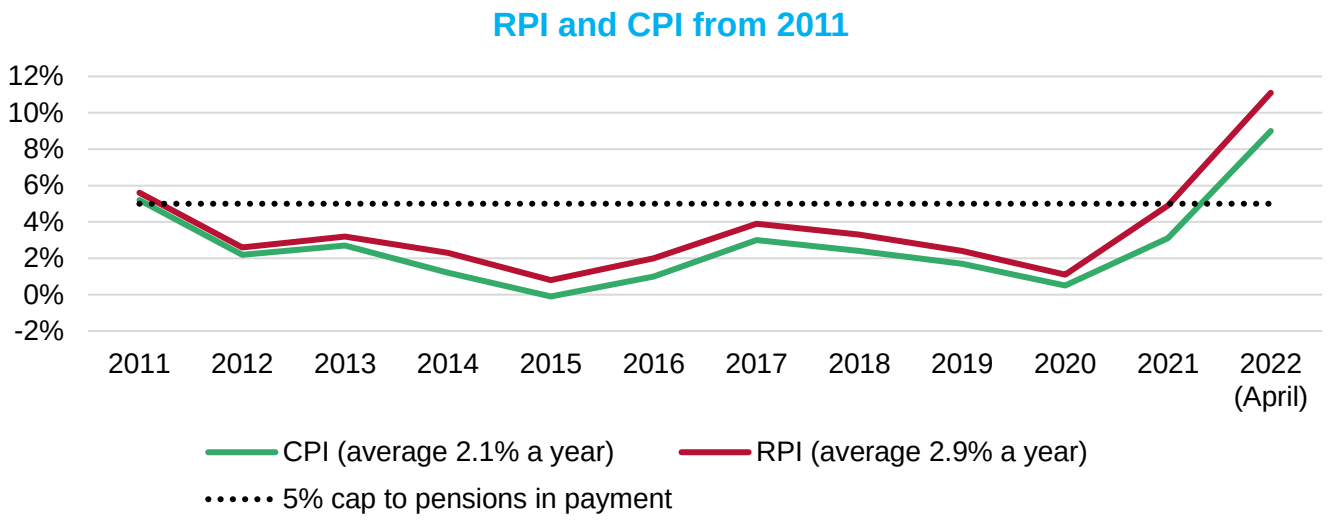
Pension increases applied to benefits earned before December 2003	What has happened in practice	What should have happened <u>if</u> the court rules against TPT
Increases applied before 2011	RPI inflation	RPI inflation
Increases applied after 2011	CPI inflation	RPI inflation

Why the inflation measure matters

Difference between RPI and CPI inflation

The choice of inflation measure can have a material impact on members' benefits. This is because RPI inflation is generally expected to be higher than CPI inflation (see our First Briefing for more information on this topic).

Annual RPI and CPI inflation are plotted on the chart below (using September as the reference date for previous years), along with a line showing the 5% cap to pension increase in payment that applied to these benefits. Over this period, the average difference between RPI and CPI has been just under 1% pa. The chart also shows the most recently available RPI and CPI inflation figures for 2022.



Impact on members' benefits

In the table below we illustrate the difference in pension a member would have received had they received RPI- or CPI-based pension increases from 2011. These figures assume an annual pension in payment of £10,000 in 2011, all earned before 2003.

Year	Annual pension *(CPI increases)*	Annual pension *(RPI increases)*	Difference (pa)	Difference cumulative
2011	10,000	10,000	-	-
2012	10,520	10,560	40	40
2013	10,751	10,835	83	123
2014	11,042	11,181	140	263
2015	11,174	11,438	264	527
2016	11,174	11,530	356	883
2017	11,286	11,761	475	1,357
2018	11,625	12,219	595	1,952
2019	11,904	12,622	719	2,671
2020	12,106	12,925	819	3,490
2021	12,166	13,068	901	4,391
2022	12,544	13,708	1,164	5,556

We can see that for this example member, using RPI inflation for pension increases:

- Results in a pension around 10% larger, and
- Results in back payments equal to around 45% of the pension in payment (before interest).

These figures illustrate the significant impact different inflation measures can have on members' benefits.

Impact on 31 March 2022 financial statements and triennial funding valuations

Financial statements at 31 March 2022

TPT have made no allowance in their online FRS102 tool for any potential increase in liabilities as a result of this issue, quoting the uncertainty of the outcome of court proceedings and difficulties in allocating liabilities for members with split-service across different employers.

TPT have prepared a note for auditors explaining this issue, as well as a draft note for financial statements.

Employers should raise this with their auditors to ensure that they agree with the approach proposed by TPT.

Actuarial funding valuation as at 30 September 2023

The next actuarial funding valuation has an effective date of 30 September 2023, with any changes in contributions arising from this valuation expected to come into force from 1 April 2025.

As the court's decision is not expected to be known until after this valuation has been concluded, TPT has confirmed that:

"It is therefore not the Trustee's intention to include the potential additional liabilities arising from the benefit review in the 2023 valuation balance sheet. However, this position is based upon current legal advice and will need to be reviewed and agreed with the Employer Committee during the consultation process for the 2023 valuation."

While it appears that there will be no allowance for any potential increase in liabilities in the 2023 actuarial valuation, this is clearly an issue that the SHPS Employer Committee will be discussing at length with the SHPS Scheme Committee. It will also be an issue for those employers that have bulk-transferred their assets and liabilities away from SHPS.

Employers should understand the potential additional deficit contributions that may arise if the court rules that more expensive benefits should be paid.

Timeline

TPT is aiming to provide employers with a copy of the proposed court documents by the end of the year, with a three-month period for employers to provide any comments if they wish. TPT has stated that, in their opinion, there is no requirement for employers to take independent legal advice, and that TPT will be presenting the case that the status quo should apply.

TPT expects to be able to share court documents with employers in Q4 2022, with Court proceedings and judgment expected in the second half of 2024.

Employers should consider whether they wish to take independent legal advice on the draft court documents.

Next steps for employers

Employers should:

- Discuss the proposed TPT approach with auditors for 31 March 2022 financial statements
- Consider whether to take independent legal advice on the draft court documents.

To discuss this briefing or any area of pensions, please contact your usual First Actuarial consultant or any of our nationwide housing specialists.