Housing briefing, June 2024
SHPS employer debts – Pay or stay?

In this briefing, we look at the options available for employers that have closed to future pension build-up (or are considering closure) and are looking to manage their historical liabilities in the Defined Benefit section of the Social Housing Pension Scheme (SHPS DB).

Haven't we covered this before?

Many employers in a Local Government Pension Scheme (LGPS) now find their admissions in a surplus position. See **our August 2023 briefing**.

Some employers in SHPS are considering their position, and are asking whether paying their 'employer debt on withdrawal' makes financial sense.

What is an employer debt?

When an employer departs from a Defined Benefit (DB) scheme they need to settle their share of any funding deficit.

In a DB scheme such as SHPS, employer debt is an estimate of the difference between an employer's asset share and the amount required to secure its liabilities (and orphan liabilities) with an insurance company. The debt is known in pension legislation as the "Section 75 debt".

The employer debt can be seen as the cost of walking away from SHPS and no longer being 'on the hook' for future deficit contributions.

We understand that SHPS employers received their 30 September 2023 debt estimates towards the end of May 2024.

How does this differ from a bulk transfer?

Several larger employers have completed a bulk transfer out of SHPS.

Under a bulk transfer, an employer's share of assets and liabilities is transferred to a new arrangement. The employer remains 'on the hook' for funding the new scheme, but has more influence over funding and investment strategy.

Due to the costs involved, bulk transfers are typically only feasible for employers with a 'critical mass' of assets and liabilities in SHPS (typically over c£15m).

Unlike with bulk transfers, employers of any size can choose to pay their employer debt (and remove all future costs and risks of SHPS DB).

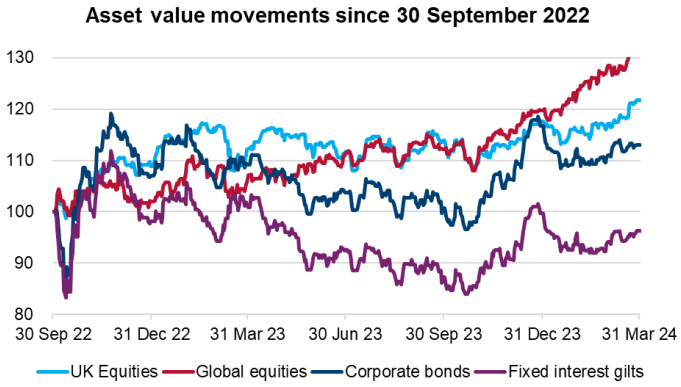
Why are employer debts being discussed now?

Employer debts are not new, but the cost has generally been prohibitive. However, the increase in long-term interest rates has significantly reduced these debts over the last two years.

The 30 September 2022 employer debts were half the size they were two years earlier.

Since then, market conditions have continued to be favourable. Consider the chart below:

- Growth assets, such as equities, are generally up by over 20%
- Long-term interest rates have continued to rise, reducing DB liabilities (but also assets to some extent).



The above asset classes are only a small sample, and in practice SHPS invests in a much wider range of assets.

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Based on market movements, we expect the latest debt estimates to have reduced further.

Once employers receive their latest debt estimate, they should assess how the costs and risks of paying this compare to remaining in SHPS.

Can boards simply write a cheque and leave?

Not quite. There is some due diligence required before paying your Section 75 debt.

Boards will want to ensure that payment of any employer debt is an efficient use of cash, and should consider how the estimated cost of remaining in SHPS could differ in future.

The impact on members is a key consideration. If any current employees still have pension benefits linked to their final salary, care needs to be taken to understand the impact of paying the debt.

Paying the employer debt also means that you will no longer be able to use the Defined Contribution (DC) section of SHPS. Employers will need to decide how to provide future DC benefits and group protection benefits.

All this makes expert actuarial and legal advice essential. We expect legal advice to consider the merits of a deed of cessation, giving employers a contractual discharge from any future liabilities (alongside the statutory discharge under Section 75).

What if we still allow future DB pension accrual?

While we've raised lots of points for consideration, there are many more issues to think about if you still have employees building up DB benefits, as this will no longer be possible once you've left SHPS.

As each situation is different, we would suggest speaking with your adviser about your options.

What about the TPT court case?

The SHPS Trustee is in the process of asking the court to rule on whether scheme benefits have been paid correctly (see our **June 2022 briefing** and **July 2022 briefing**).

The benefit review applies to all multi-employer TPT schemes, not just SHPS.

Until this is resolved, we understand that the Trustee **cannot certify the final debt amount, although employers can still crystallise their position based on market conditions at the point of exit**.

We'd expect most employers in this situation to pay a proportion of the estimated debt, with the balance paid once the benefit review is finalised – alongside any additional liabilities arising from the review.

Does this also apply to the Growth Plan?

Yes. Employers in the Growth Plan have also seen their Section 75 debts reduce due to the market movements discussed above.

The Growth Plan differs from SHPS in that a significant amount (roughly 50%) of the liabilities relate to orphan liabilities – i.e. they're not attributable to any of the participating employers.

For most housing associations, debts in the Growth Plan also tend to be much smaller in monetary terms than SHPS debts, meaning that employers may be able to 'tidy up' their pension arrangements at a relatively low cost.

What are employers doing now?

At First Actuarial, we are advising several SHPS employers on the pros and cons of paying their debt.

Some boards have taken the decision to leave SHPS, and have done so.

Others have carefully considered the options and are maintaining a 'watching brief', with the topic being periodically covered at board meetings (such as once a year when the new debt estimates are issued).

Regardless of any decision reached, boards need to consider the pros and cons of paying their employer debt.

Get in touch

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