TPR Annual Funding Statement 2024

The Pensions Regulator (TPR) has published its latest Annual Funding Statement (AFS2024). This statement is prepared for trustees and sponsoring employers of occupational defined benefit (DB) pension schemes.

It is relevant for all schemes given the impending launch of the new DB funding regime and particularly for schemes with valuation dates between 22 September 2023 and 21 September 2024 (known as Tranche 19 or T19).

It also highlights matters that should be considered for trustees of schemes in a surplus position (on either a technical provisions or buyout basis).

Background

Key messages

- Most schemes have seen material improvements in funding levels, with around half of schemes now in surplus on a buy-out basis. Less than a quarter of schemes are expected to have a deficit on their technical provisions basis.
- Where funding levels have improved significantly, trustees should review their long-term strategy and potentially align it with a target to run on and generate surplus or enter a consolidator or insurance arrangement.
- For the sizeable minority of schemes that remain in deficit on a technical provisions basis, trustees should continue to focus on setting their recovery plans to be as short as is reasonably achievable and pay careful attention to the employer covenant.
- It would be good practice for trustees to consider the steps they can take now to align (even if broadly) with the upcoming DB funding code which TPR is expecting to be publish in the summer, so as to avoid having to make significant changes at the next valuation to be compliant.

GENERAL CONSIDERATIONS FOR SCHEMES CURRECNTLY UNDERTAKING A VALUATION

In light of improved funding levels, some trustees may be faced with calls from employers for reduced contributions (potentially to subsidise the cost of future benefit accrual for open schemes) and for members for discretionary pension increases. All relevant factors should be considered by trustees, including funding level, resilience of investment strategy, level of covenant support and past practice on discretionary increases (and the rules of their scheme governing the award of such increases).

Trustees should be aware that employer covenant support remains an important consideration (particularly for open schemes, underfunded schemes and where the covenant is weak). Accordingly, sponsor-related re-financing risks, covenant leakage and equitable treatment of the scheme compared to other stakeholders (for example, payment of dividends to shareholders) remain very important matters for trustees to manage.

Trustees are reminded that the potential impacts of climate change and sustainability on investments, liabilities and employer covenant should be taken into account in their funding and investment strategies where appropriate.

RETHINKING STRATEGIES

The statement (as it did last year) groups schemes into three broad categories:

1. Funding level at/above buyout
2. Funding level above technical provisions but below buyout
3. Funding level below technical provisions

Key issues highlighted in the statement for each category are:

FUNDING LEVEL AT/ABOVE BUYOUT

- Main immediate decision will be to either set or review their long-term strategy which for most schemes is expected to be buyout or run-on (consolidation may be an option too).
- Decision/strategy should be documented along with the rationale for the decision.
- Trustees are encouraged to take sustainability into account during the buyout due-diligence phase – trustees may wish to familiarise themselves with this publication by Accounting for Sustainability on the Bulk Annuity Process sustainability principles charter for the bulk annuity process.
- If following a strategy of run-on, trustees should ensure this is a better option for members compared to alternatives e.g. due to surplus that will be generated.

FUNDING LEVEL ABOVE TECHNICAL PROVISIONS BUT BELOW BUYOUT

- Trustees should review their long-term objective and timescale for reaching it.
- Consideration may be given to emerging options e.g. consolidators, capital-backed journey plans, public sector consolidator.
- Given emerging options, a “wait and see” approach may be appropriate.
- Trustees may wish to explore options which might improve governance or benefit from greater buyout power – tPR intends to publish guidance on “DB alternatives for consolidation” later this year.

FUNDING LEVEL IS BELOW TECHNICAL PROVISIONS

- Primary focus should be on removing technical provisions deficit.
- Trustees should also ensure technical provisions remain aligned with long-term funding target.
- Risk-taking should reduce as the funding improves or as the scheme matures.

Belfast
T: +44 (0)28 9041 2000
Birmingham
T: +44 (0)121 389 2314
Bristol
T: +44 (0)117 959 5002
Glasgow
T: +44 (0)141 331 1004
Leeds
T: +44 (0)113 426 4487
London
T: +44 (0)20 7495 5505
Manchester
T: +44 (0)161 641 6312
www.spenceandpartners.co.uk