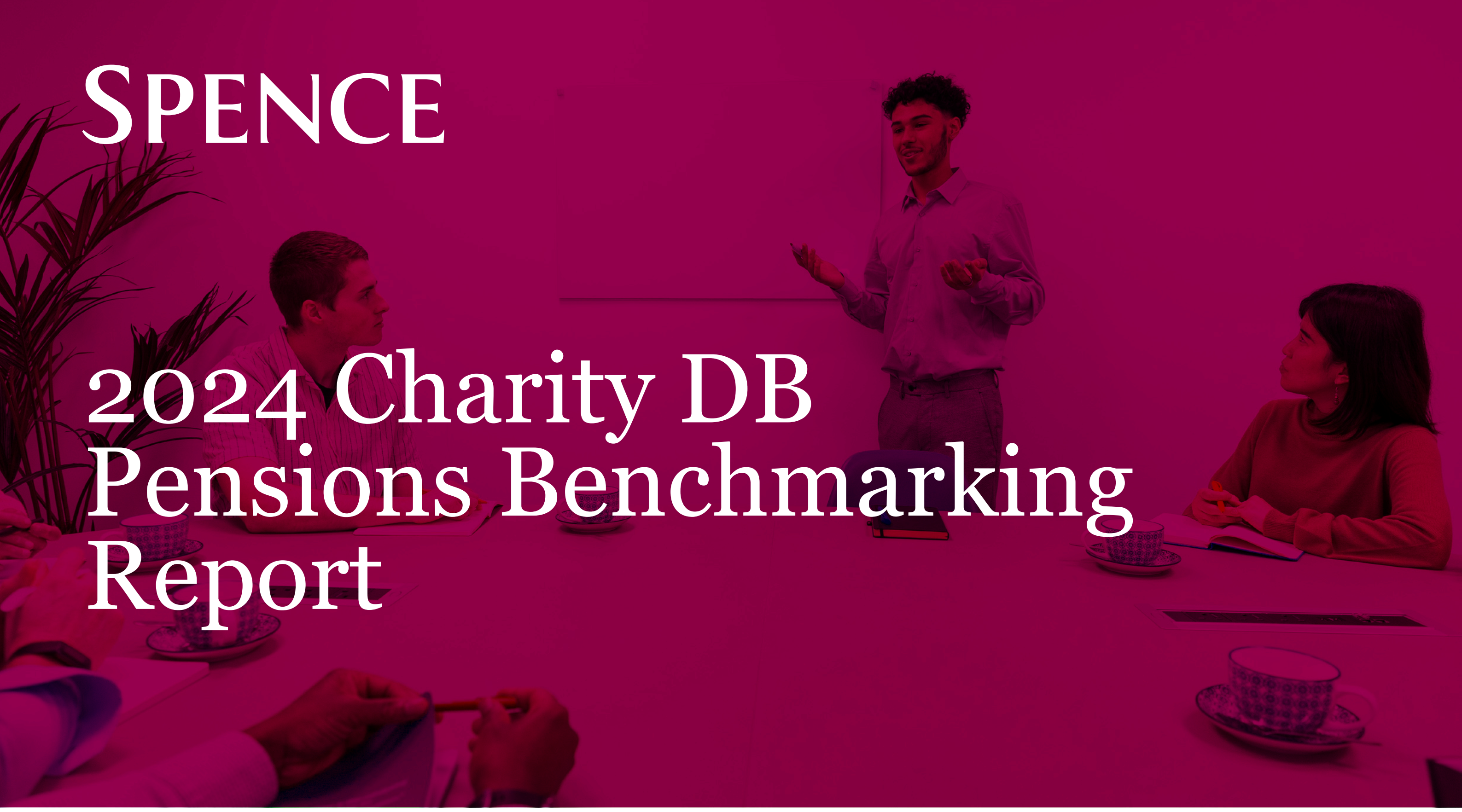


SPENCE

2024 Charity DB Pensions Benchmarking Report

Key findings

Welcome to the inaugural 2024 Spence Charity DB pensions Benchmarking Report. We've analysed the accounts of 50 charities in England & Wales with larger DB schemes, with year ends spanning 30 April 2022 to 31 July 2023. In aggregate, this covers £8.5bn of DB assets. Our key findings are:

Average funding level is 104% on an FRS102 basis and 83% on an insurance buy-out basis.	Improved funding levels means charities should now review their DB endgame plan.
DB buy-out deficits average 21% of unrestricted charity reserves.	Rising yields have shrunk DB schemes relative to charity balance sheets. Running on schemes to access a surplus may now be more viable.
26% of charities are no longer paying deficit recovery contributions.	More deficit contributions will turn off as recovery plans end, shifting focus to endgame and simplifying running costs and governance.
For those paying contributions, they average 2% of unrestricted income.	Deficit contributions remain material for charities that pay them, particularly given the low margins on charitable work.
Only 33% of charities with an FRS102 surplus are fully recognising the surplus on balance sheet.	Charities may have difficulty accessing a surplus on eventual wind-up or run-on. Needs review as part of endgame planning.
Annual running costs average £450,000 per annum.	Review operational model to reduce costs and simplify governance if costs are high.

The main picture is improved funding levels in the sector in recent years, and therefore the need to consider pension surpluses rather than pension deficits in many cases. Whilst this is welcome, it brings its own questions, challenges and considerations, such as what is our endgame plan, can we access the surplus and how do we reduce running costs and simplify the governance burden?

What should charities be doing?

1) REVIEW YOUR DB ENDGAME PLAN

Funding levels for DB schemes have improved dramatically in the last 2 years with rising yields, and we're seeing that come through in the analysis, particularly for the December 2022 and March 2023 year ends. Schemes are now on average fully funded on an FRS102 basis and therefore broadly also on a Technical Provisions basis. Charities should therefore now turn to planning the endgame for their DB schemes. For most, this still means insurance buy-out, and many are already well progressed with 18% having already completed a partial buy-in of some liabilities and 10% within 5% of full funding on a buy-out basis.

However, some charities may wish to consider run-on or deferring buy-out to generate surplus from the DB scheme and value for members and the charity. As an example, if all schemes in the survey were run on for the next 10 years, this would generate excess assets above insurance buy-out of £400m. That averages 7% of current DB assets for the schemes in this position. With years of pain, cost and liability from DB schemes, charities could potentially start viewing their schemes as an asset rather than a liability.

The excess assets generated in the pension scheme over the next 10 years equates to an average of 12% of unrestricted charity reserves or 8% of unrestricted annual income. What's more, charities don't have to pay the 25% tax on pension scheme surplus refund, having not had corporation tax relief on the pension contributions they paid historically.

2) REVIEW OPERATIONAL PROCESSES AND COSTS

As funding levels improve and deficit contributions turn off, focus turns to where value can be added in other areas, like reducing running costs and simplifying governance. Running costs for DB schemes can get very high if left unchecked, and we've seen that come through in the analysis with average running costs of £450,000 per annum. Whilst some of this is justified with data work such as the need to equalise GMPs, some of it can be removed by using the latest systems and a simplified governance model. Options to consider include:

- **Review service providers:** with continued consolidation and innovation in the provider market, review service providers to ensure you're getting the best value for money;
- **Shrink trustee boards:** with DB schemes now a legacy issue the need for large trustee boards is generally no longer there. Consider shrinking boards to 3 trustees or use a sole trustee to drive efficiencies and quicker decision making;
- **Consider packaged solutions:** many advisers and professional trustee firms now offer lower cost solutions, particularly for admin and actuarial services, which leverage economies of scale from a book of clients.

We estimate that running costs could be cut by 30% with these actions – that's an average saving of £135,000 per annum.

Get in touch

If you're involved in a DB scheme in the charity sector and want to discuss ways to address deficits, access surpluses, reduce running costs or benchmark your scheme against this analysis, then please get in touch.

Alistair Russell-Smith

Charity-Not-For-Profit / Corporate Advisory Lead

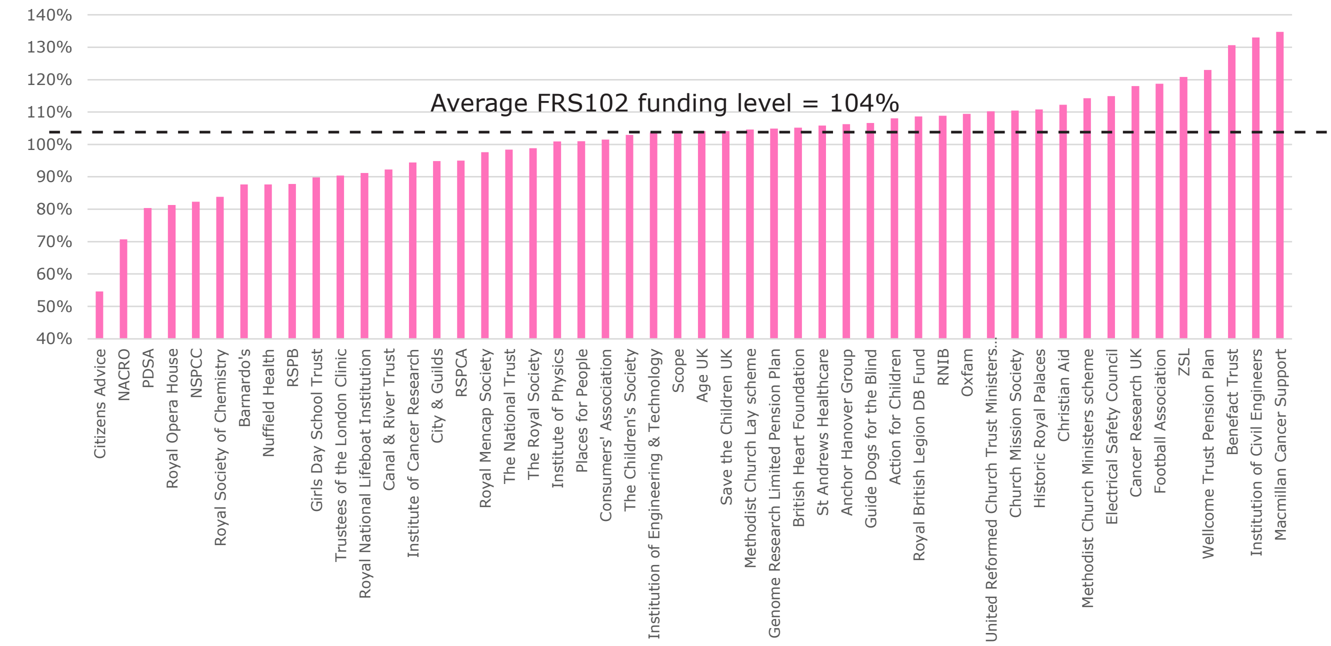
alistair_russell-smith@spenceandpartners.co.uk

020 3837 2960

The results in more detail

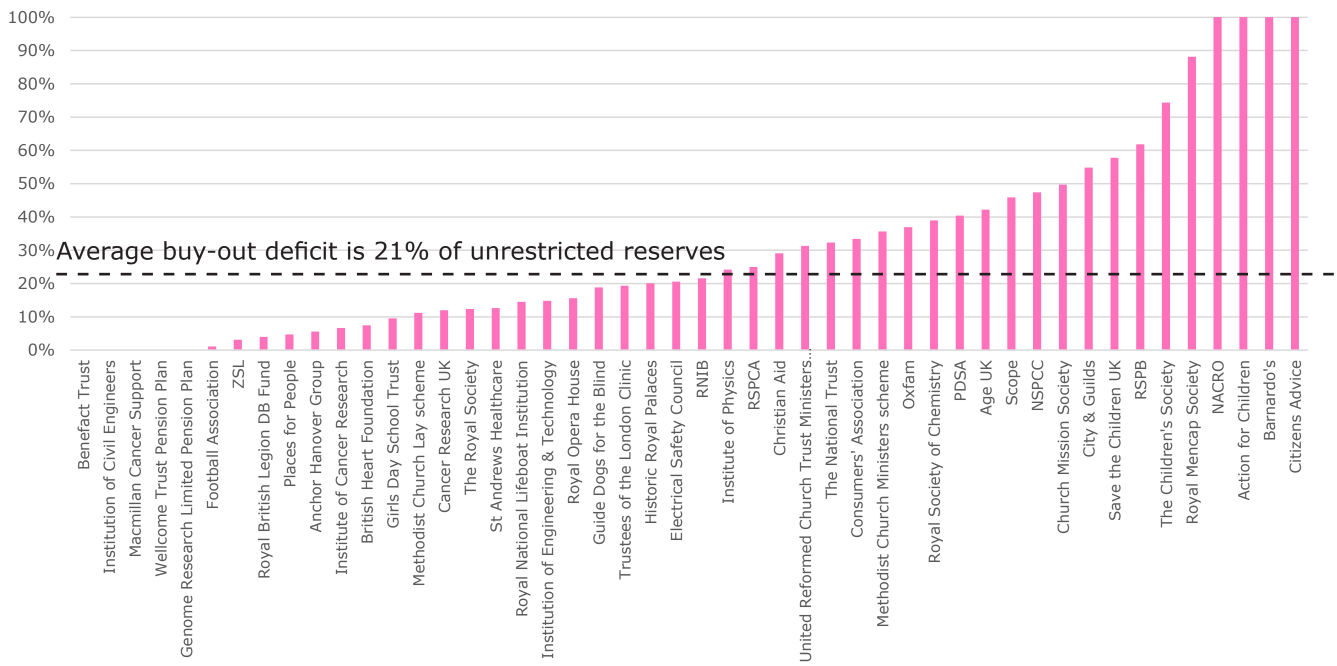
The charts below show the spread of outcomes for the different charities included in this analysis.

FRS102 FUNDING LEVEL



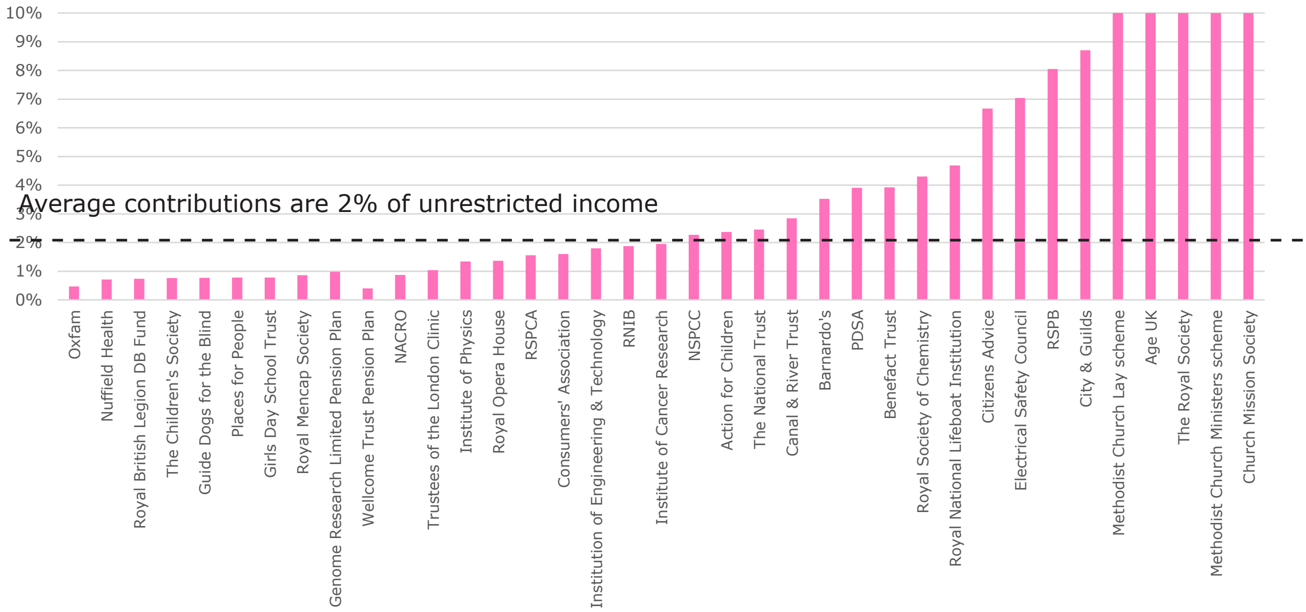
- FRS102 funding levels range from 55% to 135%
- Only 33% of the charities in surplus under FRS102 are fully recognising the surplus on balance sheet, typically because of restrictions in scheme rules on the ability for sponsors to access a pension surplus.

ESTIMATED INSURANCE BUY-OUT DEFICIT AS A PROPORTION OF UNRESTRICTED RESERVES



- Whilst most schemes are in surplus on an FRS102 basis, they remain in deficit on an insurance buy-out basis.
- The buy-out deficit is material relative to unrestricted reserves for some charities, exceeding unrestricted reserves for 4 charities.
- However, the buy-out deficit is less than 1/3rd of unrestricted reserves for 60% of charities. These are the situations where running on the DB scheme to generate an asset accessible by the charity is more viable.

DB PENSION CONTRIBUTIONS AS A PROPORTION OF UNRESTRICTED INCOME

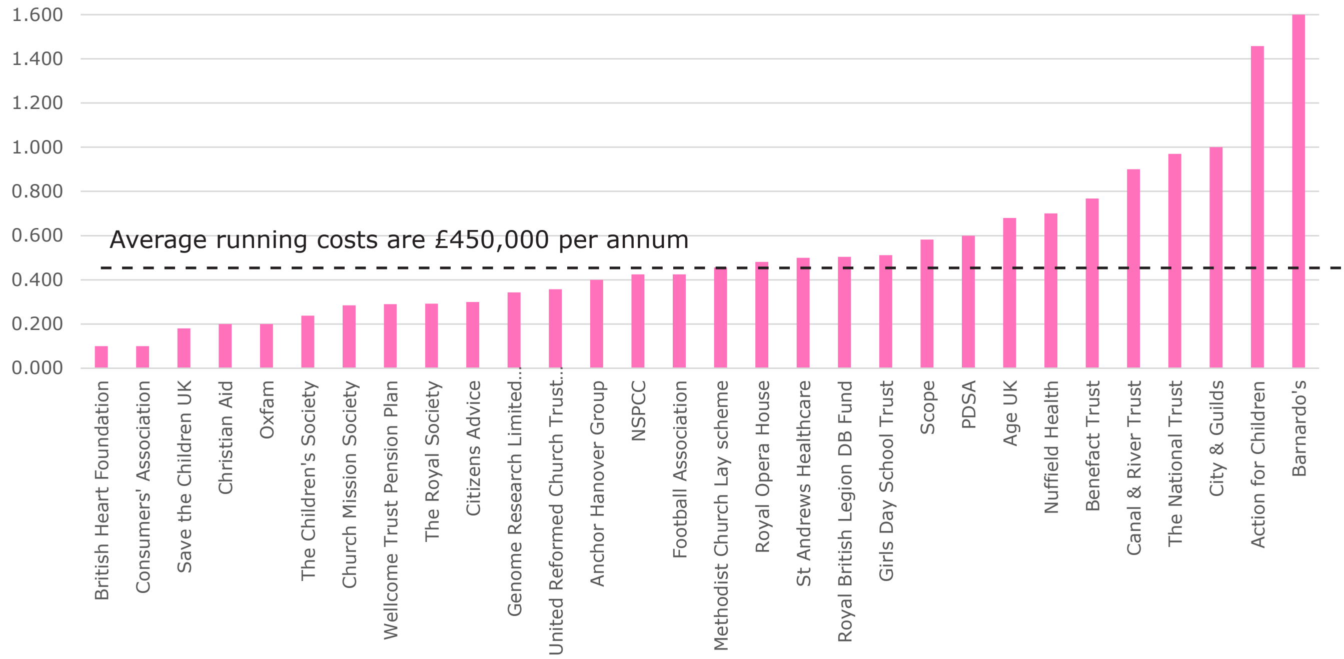


— 74% of charities are still paying deficit contributions, and they are shown above (charities paying contributions of less than £300,000 a year are excluded on the basis that this level of contributions is likely funding running costs rather than the pension deficit).

— Contributions average 2% of unrestricted income.

— A minority of charities are paying a significantly larger proportion of unrestricted income than 2%, with five paying more than 10%. Some of these higher proportions likely reflect one-off lump sum contributions rather than regular contributions at this level.

RUNNING COSTS



— 60% of the charities disclose annual running costs. Charities that did not disclose running costs likely pay expenses directly and account for this expense outside of the pension scheme.

— Average running costs are £450,000 per annum, but there is a wide range around this.

— Charities with larger running costs typically have larger DB schemes.

— Some of the charities with lower running costs are in DB mastertrusts, which typically leads to lower running costs than managing your own scheme.

LIST OF CHARITIES INCLUDED IN THE ANALYSIS

Charity	Year end	DB assets (£m)	FRS102 liabilities (£m)
Action for Children	31/03/2023	497.5	460.4
Age UK	31/03/2023	117.7	113.1
Anchor Hanover Group	31/03/2023	170.0	160.0
Barnardo's	31/03/2023	566.0	645.8
Benefact Trust	31/12/2022	311.2	238.2
British Heart Foundation	31/03/2023	40.6	38.6
Canal & River Trust	31/03/2023	398.0	431.5
Cancer Research UK	31/03/2023	506.6	429.3
Christian Aid	31/03/2023	61.3	54.6
Church Mission Society	31/01/2023	61.2	55.4
Citizens Advice	31/03/2023	60.7	111.2
City & Guilds	31/08/2022	190.0	200.3
Consumers' Association	30/06/2023	101.6	100.1
Electrical Safety Council	31/03/2023	73.8	64.2
Football Association	31/07/2022	82.9	69.8
Genome Research Limited Pension Plan	30/09/2022	295.7	282.0
Girls Day School Trust	31/08/2022	104.7	116.6
Guide Dogs for the Blind	31/12/2022	213.0	199.7
Historic Royal Palaces	31/03/2023	74.9	67.6
Institute of Cancer Research	31/07/2023	70.8	75.0
Institute of Physics	31/12/2022	76.9	76.2
Institution of Civil Engineers	31/12/2022	41.1	30.9
Institution of Engineering & Technology	31/12/2022	114.0	109.9
Macmillan Cancer Support	31/12/2022	38.0	28.2
Methodist Church Lay scheme	31/08/2022	70.0	66.9
Methodist Church Ministers scheme	31/08/2022	460.9	403.4
NACRO	31/03/2023	32.8	46.4
NSPCC	31/03/2023	116.1	141.1
Nuffield Health	31/12/2022	284.4	324.4
Oxfam	31/03/2023	169.0	154.4
PDSA	31/12/2022	92.1	114.6
Places for People	31/03/2023	175.3	173.6
RNIB	31/03/2023	185.5	170.4
Royal British Legion DB Fund	30/09/2022	55.2	50.8
Royal Mencap Society	31/03/2023	95.0	97.3
Royal National Lifeboat Institution	31/12/2022	241.9	265.2
Royal Opera House	28/08/2022	61.7	75.9
Royal Society of Chemistry	31/12/2022	74.8	89.2
RSPB	31/03/2023	173.7	197.8
RSPCA	31/12/2022	206.8	217.7
Save the Children UK	31/12/2022	144.5	138.8
Scope	31/03/2023	74.6	71.9

Charity	Year end	DB assets (£m)	FRS102 liabilities (£m)
St Andrews Healthcare	31/03/2023	136.5	129.0
The Children's Society	31/03/2023	119.1	115.7
The National Trust	28/02/2023	572.7	582.0
The Royal Society	31/03/2023	42.8	43.3
Trustees of the London Clinic	31/12/2022	77.3	85.5
United Reformed Church Trust Ministers scheme	31/12/2022	145.1	131.6
Wellcome Trust Pension Plan	30/09/2022	361.5	293.9
ZSL	30/04/2022	59.8	49.5

Methodology

We have analysed the latest published accounts of 50 charities in England & Wales with larger DB schemes. The schemes range in size from £35m to £600m of assets. The analysis focuses on standalone schemes, rather than participation in multi-employer pension schemes. Some of the charities included in this analysis do also participate in multi-employer schemes such as Local Government Pension Schemes (LGPS), the Universities Superannuation Scheme (USS) and schemes run by The Pensions Trust (TPT).

The vast majority of the data is taken directly from the charity accounts, without making any further judgements, but further detail on the approach used includes:

- Unrestricted reserves and unrestricted income of the charities are considered when assessing the size of the charity relative to the size of the pension scheme. This is on the basis that restricted funds and endowments are generally not available to support the pension schemes.
- The unrestricted reserves considered are prior to the deduction of any DB deficit or addition of a DB asset for the standalone schemes in this analysis (any reserves adjustment for any other pensions exposures outside of this analysis has been retained).
- Insurance buy-out liabilities are estimated by applying a 25% uplift to the disclosed FRS102 liabilities. This is intended to be a broad proxy for the cost of buy-out, but does not reflect scheme specific circumstances and maturity.
- For estimating the level of surplus assets above insurance buy-out that could be accessible over the next 10 years, we have assumed a return on scheme assets of Gilts + 1.5% pa, intended to be an expected return for a typical run-on investment strategy and similar to the returns targeted by insurers.
- Some charities are excluded from some metrics either because the data was not disclosed (for example with scheme running costs) or because of specific quirks relating to some metrics (for example some charities do use restricted funds or endowment funds to support the pension scheme).

About Spence & Partners

The charity and not-for-profit practice at Spence & Partners has a 20 year track record of delivering pensions advice, and is recognised as one of the pre-eminent pensions advisers in the sector. We have advised 100s of charities and not-for-profit organisations on pensions.

Spence & Partners use the proprietary pensions software Mantle for advising and administering DB schemes. This integrated actuarial, administration and investment system fully automates processes and removes the need to transfer data from one system to another, significantly reducing running costs for schemes.

3173 Group owns Spence & Partners and Dalriada Trustee Limited. The two companies are operationally separate. Spence & Partners work with a wide range of independent trustee firms. Where Spence & Partners are appointed as an adviser to an ongoing scheme, it is not possible for Dalriada to be a trustee to that scheme (and Spence will not accept an appointment to act as adviser to an ongoing scheme where Dalriada is trustee)

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