

Are you a passenger to your pension scheme's destination?

All schemes are now required to have a long-term funding and investment strategy. Now is the opportune time for employers to proactively engage with trustees to steer the conversation towards its desired objectives. Understanding your preferred long-term strategy and engaging early with trustees is therefore crucial.

This edition of XPS Express is the **second in a series on setting long-term strategies** – read part **one** [here](#).

At a glance

Employers and trustees are required to agree a formal funding and investment strategy for the first time, including setting a long-term objective for their scheme.

If employers do not take the lead on establishing the appropriate long-term strategy, trustees may decide on one that does not meet the employers' objectives.

This could result in a more expensive or longer journey for the employer, actions needing to be reversed or even stop employers achieving their desired goals.

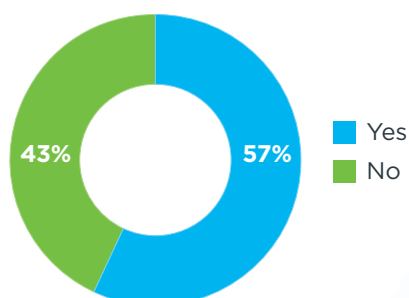
Early engagement is therefore key to ensure all parties are navigating towards the same desired destination.

Buyout versus run on

Given recent funding improvements, many schemes are close to or above buyout funding levels, but our survey suggests there is considerable appetite among employers to run on.

Whilst the decision to run on can be revisited at a later date, buyout is a one-off decision, which should be considered carefully.

Q: Would you look to run on?



Source: XPS survey, response to a question asking employers whether they would look to run on if the Government introduced a statutory override to allow employers to receive refunds of surplus.

Choosing whether to run on

Risks	Opportunity
• Higher costs	• Surplus return
• Reputational	• Lower future costs
• Accounting loss	• Improve member outcomes

Ways to tip the balance:

- Know desired long-term strategy
- Understand risks and how they can be mitigated
- Monitor position regularly

Actions employers should take

1. Understand the pros and cons of different long-term strategies. XPS can produce quantitative analysis to help you compare the possible options.
2. Decide on the appropriate long-term strategy.
3. Discuss long-term strategy preference with the trustees and understand how this aligns with the Funding and Investment strategy. XPS can help with putting a robust strategy in place that supports your objectives.
4. Monitor the position and regularly reassess to ensure the desired long-term strategy remains the optimal outcome for you.

Long-term strategy options

There are four key long-term strategies to choose from, all of which come with potential upsides and downsides. There are a number of key considerations for employers to consider when deciding on their preferred long-term strategy.

Key considerations that may impact your choice of long-term strategy

- **Time:** How long are you willing to support the scheme?
- **Cost:** What level of financial support are you willing to put into the scheme?
- **Risk:** How much risk are you willing to shoulder?
- **Outcome preference:** What is your desired outcome? Do you need to generate a cashflow? Remove the scheme from the balance sheet?
- **Other:** Are there other accounting implications or active members to consider?

- Weak funding level
- Moderate funding level
- Strong funding level



Insurance

- ✓ Risks removed
- ✗ High costs
- ✗ Irreversible
- ✗ Accounting implications?

Run on for surplus

- ✓ Surplus release
- ✓ Could insure later
- ✗ Risks need managing

Consolidators

- ✓ Weaker covenants
- ✓ Cheaper insurance
- ✗ Irreversible
- ✗ Relatively untested

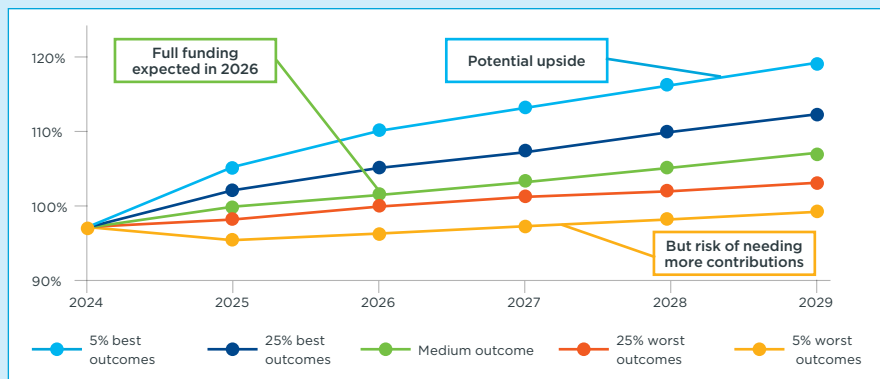
Run on (on low dependency)

- ✓ Reduced ongoing risk
- ✓ No fee
- ✓ Could insure later
- ✗ No surplus release

Case study:

XPS recently supported an employer with a £1bn+ Scheme that had a 3% funding shortfall on a solvency basis. The employer ruled out consolidators and run on (on low dependency) and wanted to avoid injecting a large cash lump sum to secure buyout, but wanted to understand the potential revenues and risks of running the scheme on for surplus.

Our scenario analysis showed the following range of outcomes:



Outcome:

- Our analysis helped the employer conclude that the risks were too great to run on over the longer term as a standalone entity.
- The analysis showed there was merit in running on over the shorter term to avoid the need for injecting cash.
- We helped the employer propose alternative covenant to support this journey.

Find out more

For further information, please get in touch with **Charlotte Yuen**, **Jamie Hunter** or **Dan Auton** or speak to your usual XPS Group contact.



Charlotte Yuen
Senior Consultant

charlotte.yuen@xpsgroup.com



Jamie Hunter
Senior Consultant

jamie.hunter@xpsgroup.com



Dan Auton Head of
Corporate Solutions

dan.auton@xpsgroup.com

© XPS Group 2024. XPS Pensions Consulting Limited, Registered No. 2459442. XPS Investment Limited, Registered No. 6242672. XPS Pensions Limited, Registered No. 3842603. XPS Administration Limited, Registered No. 9428346. XPS Pensions (RL) Limited, Registered No. 5817049. XPS Pensions (Trigon) Limited, Registered No. 12085392. Penfida Limited, Registered No. 8020393. All registered at: Phoenix House, 1 Station Hill, Reading, RG1 1NB.

XPS Investment Limited is authorised and regulated by the Financial Conduct Authority for investment and general insurance business (FCA Register No. 528774).

This communication is based on our understanding of the position as at the date shown. It should not be relied upon for detailed advice or taken as an authoritative statement of the law.