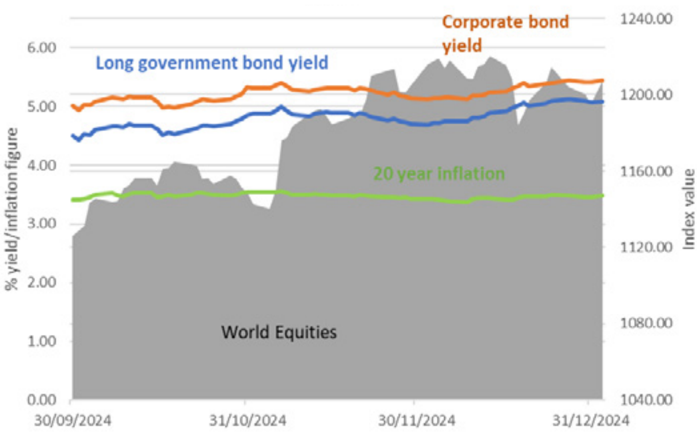
Broadstone

Employer Briefing

January 2025

Update on financial markets affecting DB pension schemes

Key market statistics 30 September 2024 to 31 December 2024



	30 Sep 2024	31 Dec 2024
Government bonds (20yr)	**4.50%**	**5.07%**
Corporate bonds (15yr AA)	**5.01%**	**5.42%**
RPI inflation (20yr)	**3.41%**	**3.46%**
FTSE All World (ex UK) Total Return Index	**1125.84**	**1194.95**

There has been a significant increase in corporate and government bond yields over the quarter. Equity markets have also increased over the period while long-term inflation expectations have risen only slightly. As a result, the majority of schemes are likely to have seen an improvement in their funding positions over the quarter. This will also have a beneficial impact on year-end accounting disclosures.

Government and corporate bond yields remain high, and the funding positions of many Defined Benefit (DB) schemes are still improved compared to historic positions. Sponsors and trustees should be proactively discussing investment strategy and long-term plans to ensure that any funding gains are protected. Insurance companies remain busy, preventing some schemes from being able to proceed with buy-out in the short term so it is still important to take actions to protect funding positions in the meantime.

With many companies disclosing financial results at the 31 December year end, we are seeing a particular focus from auditors on the recent Virgin Media vs NTL (section 37) court case and the potential additional liabilities that this could incur for schemes. This is likely to require additional work and costs for advisors and companies to address these queries and agree on how any potential impact should be reported.

DB surplus: Is a refund the best use of this money?

2024 was an eventful year. Gilt yields rose significantly which positively impacted the funding position of many DB schemes. In addition, the tax that could be applied for returning surplus funds to the employer was reduced from 35% to 25%. 2025 has continued this trend with the recent Government announcement that future legislation could allow wider access to surpluses before a scheme is wound up. These changes will be subject to consultation for some time though, so the focus remains on schemes with surpluses looking to buy out with an insurer and then wind up.

A sensible first step for employers in the fortunate position of having built up a significant surplus and in the process of buying out the scheme with an insurer is to check the DB scheme's rules to assess the company's ability to receive refunds and understand the mechanism for this occurring. For instance, the rules may provide for benefit increases to member pensions first.

Many employers will have been paying considerable deficit contributions in recent years and the chance of accessing these funds must be an exciting prospect, but it is worth taking some time to consider the value in using the surplus to fund future employer contributions to a Defined Contribution (DC) pension instead.

Using a DB surplus in this way is nothing new and has been an option for some time. With the regulatory pressure growing for DC funds to deliver sustainably improved returns, now is perhaps the time to look at DC pensions as an optimum use of surplus funds. If a paternalistic culture exists, or is one you are keen to cultivate, then the surplus could even be used to top-up contributions to a DC pension as well as, or instead of, covering the regular employer contribution.

How this could work in practice will depend upon how any DC funds may currently be managed and if they sit within or outside of your own trust-based arrangement. You may be aware of the regulatory pressure being applied to sponsors of such DC arrangements to evidence value or to consolidate into the scaled funds of a larger DC scheme such as a Master Trust. Participation within a DC Master Trust does add an extra consideration to the conversation but should not preclude the conversation from taking place. A number of DC Master Trusts have developed processes to support trustees and corporates with the use of surplus funds arising from DB schemes.

If you are in a position where this may be a real consideration and you wanted to discuss and understand more about your options, then please do not hesitate to get in touch with your usual Broadstone contact or by e-mailing **corporate@broadstone.co.uk**

Find out more

For more information on how Broadstone can help you, please contact your Broadstone consultant or use the details below.

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