Sackers

New interim regulatory regime for Superfunds

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Introduction

On 18 June 2020, TPR launched a new interim regulatory regime for DB consolidator superfunds (and other new models), pending the establishment of a full legislative framework. The new guidance, which came into effect immediately, establishes the "high bar" TPR expects new superfunds to meet to ensure both savers and the PPF are adequately protected.

Key points

- The guidance is intended to cover how trustees of a superfund's pension scheme should approach managing the funding and governance risks associated with this model. It also explains how they will be assessed and regulated.
- Updates to TPR's separate guides for trustees and employers contemplating a move to a superfund will follow, but TPR is clear that every such transfer must go through its clearance process.
- The guidance does not cover special purpose vehicle ("SPV") models which were in place before its publication date.
- Having consulted on proposals in December 2018 (see our Alert), the DWP is developing a legislative framework for the authorisation and supervision of superfunds.

What is a superfund?

According to TPR, a superfund is a model that allows for the severance of an employer's liability towards a DB scheme, where one of the following conditions applies:

- the scheme employer is replaced by an SPV employer (a shell employer put in place to preserve the scheme's PPF eligibility)
- the liability of the scheme employer to fund the scheme's liabilities is replaced by an employer backed by a capital buffer (generally created by investor capital and contributions from the original employers).

The replacement employer (backed by a capital buffer) will usually support a consolidator scheme which will have the following key features:

- acceptance (via bulk transfer) of the liabilities of a number of schemes from unconnected transferring employers

- its own governance and administration (in-house or outsourced)
- one trustee board.

TPR advises all potential superfunds to liaise with it early to check whether this guidance will apply to them.

Guidance

Whilst TPR believes DB superfunds have the potential to offer benefits for both members and sponsoring employers, such as economies of scale and good governance, it also acknowledges possible funding, personnel and governance risks inherent in the model.

In brief, to help manage these risks, TPR wants to ensure that:

- the pension scheme and its capital buffer meet certain requirements. Capital adequacy is one of the most important areas of TPR's interim regime, because under the superfund model for DB schemes there will be no employer covenant. The "overarching objective" of TPR's capital requirements is for there to be a very high probability of members' benefits being paid in full
- key individuals who exert financial control, influence the superfund's strategies, or have control over the assets, should be fit and proper (including being financially sound, and possessing the right level of knowledge, skills and experience to carry out their roles)
- the governance, systems and processes associated with the capital buffer and the scheme are appropriate and robust. For example, superfunds must comply with relevant sections of the UK Corporate Governance Code, ensure careful risk management, and focus on their investment governance. In the coming months, TPR will publish more detail on the information it requires in this area, including in relation to data, cyber security, administration tasks and processes, and trustee board oversight.

Assessment and supervision

As with the DC master trust model, TPR will perform initial and ongoing assessments of superfunds.

TPR expects superfunds and their trustees to explain how they meet its expectations before transacting, submitting information to TPR to demonstrate their approach to addressing the areas covered by the guidance.

The guidance is not prescriptive, and TPR is "open to considering other ways trustees can demonstrate they meet" its expectations. However, if trustees are unable to demonstrate that they have a satisfactory alternative means of meeting the expectations, TPR will rely upon its guidance in taking regulatory action.

TPR's ongoing regulation will require superfunds' continued engagement. This will include reporting both on a regular basis and in relation to a range of significant events or changes. More detail is promised on TPR's reporting expectations in the coming months.

Transactions and clearance

A key aspect of TPR's supervision of superfunds is the scrutiny of transfers. In particular, TPR does not expect a superfund to accept a transfer from a ceding (ie transferring) scheme that has the ability to buy out, or which is on course to do so, within the foreseeable future (five years being the example given). This is consistent with the "gateway" proposals in the DWP's consultation.

Transferring employers will need to apply for clearance in relation to a transfer from their scheme to a superfund. This will be a new category of Type A clearance event. As part of any clearance application, TPR will expect to see evidence of a transferring trustee's due diligence. The guidance also sets out the information prospective transferring schemes should expect to receive from the superfund, including full and transparent details of their offering, associated fees, and their funding and investment objective.

Guidance for transferring trustees and employers

TPR reminds trustees that they will need to be certain that a transfer to a superfund is in their members' best interests, and that they should only consider using a superfund (or similar new business model) once it has been assessed by TPR.

The new guidance also links to existing guides for employers and trustees considering transfers to superfunds. These guides will be updated "in due course" to provide "more details on what schemes and employers need to consider when transferring assets and member liabilities to a superfund". Currently, they cover the requirement to obtain clearance, evidencing the rationale that a transaction is in members' interests (and that any detriment to the scheme is mitigated), and the importance of obtaining legal, actuarial and independent covenant advice.

Regulatory action

The guidance provides TPR with a firmer basis for taking regulatory action against a superfund, where necessary and proportionate.

TPR intends to apply its expectations consistently across all the market entrants, having developed tools to allow it to independently and consistently assess the risks to members' benefits. However, any assessment against its expectations "should not be used as evidence for any other purpose, including any statutory or regulatory processes that may be introduced in the future for superfunds".

Finally, nothing in this new guidance affects TPR's ability to use its anti-avoidance powers. Although there is not yet a specific legislative authorisation framework for superfunds, TPR emphasises that all of its existing powers over occupational pension schemes remain at its disposal.

Next steps

As the superfunds market is evolving, TPR intends to develop its guidance accordingly. More detail will be provided in certain areas (for example, the enforceable protections it expects to see in the suite of a superfund's governing documentation and arrangements) in the coming months.

It will work with the Government to keep the operation of the interim regime under review, and will act if changes are required.

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