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Research Briefing

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Pensions: defined benefit superfunds

Summary
1 Background
2 The case for consolidation
3 Developing proposals and regulations for superfunds
4 Current assessment process for superfunds
5 Comment and debate

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Summary

What is a superfund?

Defined benefit (DB) schemes pay a promised pension which is based on factors such as salary and length of service. In a DB scheme the sponsor is responsible for ensuring that the scheme has enough assets to pay the benefits it has promised. If a sponsor wants to end its liability for the scheme, it can seek to transfer a DB scheme to a superfund with the agreement of the scheme trustees and clearance from the Pensions Regulator. A superfund is a consolidator body which replaces sponsoring employers with additional assets held in reserve (a capital buffer). The capital buffer may be provided by investors seeking profit and a payment from the sponsoring employer ending its liability. The Minister for Pensions and Financial Inclusion said that to "enter a superfund, sponsoring employers are required to pay a significant, upfront sum to improve the funding level of their scheme, in exchange for discharging their pensions liabilities."

Traditionally, a sponsor that wanted to end its liability for a pension scheme purchased an insurance product at a premium. A sponsor's liability may also end if it becomes insolvent.

Superfunds can be defined as the highest level of consolidation between different schemes. Lower levels of consolidation between schemes include sharing services and pooling assets. The Government is generally in favour of pension schemes consolidating. Smaller pension schemes have been seen in general as more costly and less efficient to run than larger schemes (PDF).

Developing proposals and regulations for superfunds

Under current legislation, superfunds are treated the same as other trust-based DB schemes. In December 2018, the Government put forward detailed proposals for the regulation of superfunds in a consultation.

A Pension Schemes Bill (now the Pension Schemes Act 2021) was introduced in the House of Lords in January 2020 without provisions for superfunds. During the passage of the Bill, the Minister for Pensions and Financial Inclusion Guy Opperman MP said that the "Government must bring forward legislation in respect of superfunds in the fullness of time" having earlier explained that the complexity of the required legislation will take time and require "at least a

50-clause Bill". At that point two superfunds, Clara and the Pensions Superfund, had been established, though neither was yet active.

Interim regulatory regime

In the absence of legislation and with two potential superfunds established the Pensions Regulator undertook a "targeted consultation" looking at capital adequacy, value extraction and investments. It said that it would take an interim approach to superfunds until there is a legislative regime.

In June 2020 the Pensions Regulator published guidance for DB superfunds, following the response to its consultation. Superfunds are expected to complete an assessment process with the Pensions Regulator before they can accept the transfer of a scheme. Although there was no specific legislative authorisation framework for superfunds, the Pensions Regulator explained that it could use its existing powers if funding, personnel or governance of a superfund was not fit for purpose. The first superfund, Clara-Pensions, completed its assessment process in November 2021.

Initially superfunds will not be able to make a profit, unless member benefits are bought out in full with an insurer. If legislation is still not in place, the Pensions Regulator will review its decision within three years (by June 2023).

Comment and debate

The key debates about superfunds have focussed on:

- The appropriate body to regulate superfunds.
- Whether superfunds provide an alternative to buy-out with an insurer. A buy-out involves an insurer taking full responsibility for guaranteeing the benefits of a pension scheme for all its members.
- The regulation of superfunds before a legislative framework is in place.

1 Background

There are two main types of pension schemes in the UK.[1] These are:

- **Defined benefit schemes** pay a promised pension which is based on factors such as salary and length of service. A sponsor, which is usually an employer, guarantees the promised benefits are paid. The promised pension usually provides an income for life and may also include a lump sum at retirement.
- **Defined contribution schemes** do not provide a guaranteed pension and instead provide a pot of money which can be used in retirement. The value of the pension pot can increase or decrease depending on factors, including investment returns and contributions made.

In a defined benefit (DB) scheme the sponsor is responsible for ensuring that the scheme has enough assets to pay the benefits it has promised. If a sponsor wants to end its liability for the scheme, it can seek to transfer a DB scheme to a superfund with the agreement of the scheme trustees. A superfund is a consolidator body which replaces sponsoring employers with additional assets held in reserve (a capital buffer).[2] The capital buffer may be provided by investors seeking profit and a payment from the sponsoring employer ending its liability.[3]

The Minister for Pensions and Financial Inclusion, Guy Opperman said on 18 June 2020 that:

> A superfund is a privately funded "for profit" consolidation vehicle, which takes over responsibility for defined benefit pension schemes liabilities from the sponsoring employer. To enter a superfund, sponsoring employers are required to pay a significant, upfront sum to improve the funding level of their scheme, in exchange for discharging their pensions liabilities.[4]

Under current legislation, superfunds are treated the same as other trust-based DB schemes.

Traditionally, a sponsor that wanted to end its liability for a pension scheme purchased an insurance product at a premium (see Box 1 below). A sponsor's liability could also end if it became insolvent. In these cases, the scheme would be assessed by the Pension Protection Fund (PPF). The scheme would

[1] The Pension Schemes Act 2021 allowed for a third type of scheme known as collective defined contribution or collective money purchase. More details on these schemes are covered in the Commons Library briefing Collective Defined Contribution (CDC) Schemes (CBP 8674)

[2] DB superfund guidance, The Pensions Regulator, June 2020

[3] As above

[4] HCWS301 18 June 2020

then either enter the PPF with pension payments to members typically being reduced or, if it had sufficient assets, members' pension benefits could be secured at a level above that offered by the PPF.

Box 1 What insurance options are there for pension schemes?

A **buy-in** is an insurance policy which covers the benefits promised to some of a pension scheme's members. This normally involves transferring the assets required to meet the expected cost of providing the benefits to the insurer with the payment of an additional insurance premium.

A **buy-out** involves an insurer taking full responsibility for guaranteeing the benefits of a pension scheme for all its members.

A **longevity swap** is a contract which offsets the risk of pension scheme members living longer than expected. The scheme makes regular payments based on assumed life expectancy to an insurer and the insurer pays amounts based on actual mortality.

The Government is generally in favour of pension schemes consolidating.[5] There are options for schemes to consolidate to a greater or lesser extent, for example by sharing administrative services or an investment strategy. A superfund goes beyond previous types of consolidation by allowing the sponsor of a DB scheme to end its liability for the scheme and be replaced by a capital buffer.[6]

5 Consultation outcome: Improving outcomes for members of defined contribution pension schemes, Department for Work and Pensions, 21 June 2021, Chapter 2: Encouraging consolidation

6 DB superfund guidance, The Pensions Regulator, June 2020

2 The case for consolidation

Nearly 75% of DB scheme memberships are in pension schemes with more than 5,000 members.[7] These large schemes account for less than 7% of the total number of DB schemes and 80% of DB schemes have fewer than 1,000 members.[8]

Smaller pension schemes have been seen in general as more costly and less efficient to run than larger schemes.[9] In 2014 the Pensions Regulator calculated that the average annual cost of running a DB scheme with fewer than 100 members was over £1,000 compared to £182 for schemes with more than 5,000 members.[10] In September 2018, the Pensions Regulator said that its research showed smaller schemes tend to display poorer governance standards and generally scored lower than larger schemes on trustees' adherence to the principles of the Regulator's DB code.[11]

2.1 Aggregator fund

The Work and Pensions Committee recommended in December 2016 that the Government should remove "regulatory and other barriers to scheme consolidation."[12] Its report also looked at the case for a statutory aggregator fund. It noted that a sponsor may be unable to end its liability for a DB scheme if a buy-out was prohibitively expensive and an aggregator run by the Pension Protection Fund could be an alternative for small schemes.[13] The Committee recommended that the Government consult on:

- how continued funding for the aggregated schemes should be secured;
- the nature of clearance required for sponsor contribution plans and to ensure consolidation was in the interests of members;
- which schemes would be eligible, including whether it should be restricted to closed schemes or schemes under a certain size limit; and

7 The Purple Book 2021, The Pension Protection Fund, December 2021, p7
8 As above
9 For example, DB research response (PDF), the Pensions Regulator, September 2018
10 Defined benefit (DB) scheme running cost research (PDF), The Pensions Regulator, April 2014, p4
11 DB research response (PDF), the Pensions Regulator, September 2018, p2
12 Work and Pensions Committee, Defined benefit pension schemes, 21 December 2016, HC55, para 37
13 As above, para 41

- whether a uniform benefit structure would be required and, if so, how this could be achieved.[14]

The Government did not formally respond to the report as many of the recommendations were addressed in the Department for Work and Pensions' February 2017 green paper Defined benefit pension schemes: security and and sustainability. In a the then Pensions Minister Richard Harrington said that the Government was "minded to set a framework to allow the industry to innovate" and there was "insufficient evidence of market failure" for a new public sector vehicle.[15]

2.2 Superfunds

In March 2016, the Pensions and Lifetime Saving Association, an industry body, set up a taskforce to make recommendations on the future of DB pension schemes. The taskforce's second report, The Case for Consolidation published in March 2017, recommended legislation to support the creation of superfunds:

> Government should bring forward legislation that removes barriers to consolidation. In particular, further work should be undertaken to build a regulatory framework for the creation, authorisation and supervision of Superfunds, which can absorb existing schemes and that permit employers to discharge their obligations in respect of transferring benefits.[16]

The Department for Work and Pensions published a White Paper, Protecting defined benefit pension schemes in March 2018 which included consultation on superfund proposals.[17]

The report defined superfunds as the highest level of consolidation between different schemes. The lower levels of consolidation between schemes including sharing services and pooling assets.[18] The next level of consolidation is a single governance model, where all schemes are governed as one but retain their links to their separate sponsoring employers.[19]

14 Work and Pensions Committee, Defined benefit pension schemes, 21 December 2016, HC55, para 42
15 Letter from Richard Harrington to Chair re Work and Pensions Select Committee's report on Defined Benefit pension schemes (PDF), Work and Pensions Committee, 20 February 2017
16 The Case for Consolidation, The Pensions and Lifetime Savings Association, March 2017, p37
17 Department for Work and Pensions, Protecting Defined Benefit Pension Schemes, CM 9591, 19 March 2018
18 As above, p13
19 As above

3 Developing proposals and regulations for superfunds

3.1 Consultation on the consolidation of defined benefit pension schemes

In March 2018 the Department for Work and Pensions published a White Paper, Protecting defined benefit pension schemes.[20] The paper highlighted potential benefits of superfunds giving sponsoring employers an alternative way for them to end their liability towards a DB scheme without reducing member benefits.

In December 2018, the Government put forward detailed proposals for the regulation of superfunds (described as defined benefit consolidators) in a consultation Consolidation of defined benefit pension schemes.[21] The Government is yet to respond to the consultation which closed on 1 February 2019.

The Government outlined four factors which might improve the chances of a pension scheme paying benefits in full, and avoid entering the PPF, as part of a superfund:

- the injection of additional funds from the employer or its parent group
- the capital buffer provided by a superfund's investors
- the efficiencies of scale offered by a consolidation vehicle
- the absence of potential future sponsoring employer insolvency[22]

There were a number of areas, particularly those which had similarities to existing insurance regulation, where the Government had not reached a settled position.

The consultation proposed that schemes within a superfund continue to be classed as occupational pension schemes, but that the sponsoring employer would be replaced by a capital buffer.[23]

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20 Department for Work and Pensions, Protecting Defined Benefit Pension Schemes, CM 9591, 19 March 2018

21 Consolidation of defined benefit schemes, Department for Work and Pensions, 7 December 2018

22 As above, para 5

23 As above, para 8

The Pensions Regulator authorisation and gateway

The Government proposed that the Pensions Regulator assess whether a defined benefit consolidator:

- has a viable business model
- is financially sustainable
- is well governed
- has a high probability of being able to pay members' benefits as they fall due[24]

Before entering a DB consolidator schemes would need to pass a regulatory gateway. The gateway excluded schemes with the ability to buy-out within the next five years and required evidence that transferring would increase the change of the scheme's members receiving full benefits.[25]

Financial adequacy

The Government proposed a framework where DB consolidators demonstrated that their model was based on a high probability of success. It suggested this might be demonstrating "at least a 99% probability of paying or securing all members' benefits in full."[26]

Schemes reaching buy-out

The Government did not take a view on whether or not DB consolidators should try to secure a buy-out with an insurance company at the earliest possible opportunity.[27] The Government acknowledged that if this was a requirement then a DB consolidator could be set up in such a way (for example, by paying profits to investors) to ensure that the scheme never has a realistic chance of having enough funds to secure buy-out.[28]

No member-nominated trustees

There is a current requirement that at least one third of the membership of the trustee board of a pension scheme must be member-nominated.[29] The Government did not propose to apply this requirement to DB consolidators, explaining that these could comprise very different members with different

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24 Consolidation of defined benefit schemes, Department for Work and Pensions, 7 December 2018, para 26
25 As above, para 205
26 As above, para 89
27 As above, para 117
28 As above
29 Pensions Act 2004, s241-243

benefit structures. Instead, the Government proposed a requirement to establish member panels.[30]

Triggering events

The Government's consultation proposed a series of additional trigger events, which would cause action to be taken against DB consolidators:

Tier 3: Profits cannot be taken

The consultation considered options to test whether a DB consolidator would be eligible to draw profits.

If the applicable test was failed then the consolidator would be unable to draw profits.[31]

Tier 2: Prevent new business being written

The Government proposed that if the DB consolidator no longer meets the funding level requirements for authorisation it would be able to keep running existing schemes but not take new ones – subject to Tier 1 and minimum funding levels not being breached.[32]

Tier 1: pay any remaining capital buffer into the scheme and enable a transfer to another consolidator or to wind up above minimum Pension Protection Fund levels

The Government proposed that if the funding level fell to less than 90% of the authorisation basis (or a broadly equivalent measure) then any remaining capital buffer should be paid into the scheme and the trustees should seek to transfer the members to a new superfund.[33]

Minimum funding level: the scheme must be wound up

The Pension Protection Fund pays compensation to members of DB pension schemes when a sponsoring employer becomes insolvent and the scheme does not have enough assets to pay members at a level equivalent to PPF compensation. The Government proposed that if the funding of a scheme in a DB consolidator fell to a level slightly above (for example 5%) that which would be required to guarantee the amount paid by the PPF if the scheme became insolvent, then an automatic winding up of a DB consolidator would be triggered.[34]

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[30] Consolidation of defined benefit schemes, Department for Work and Pensions, 7 December 2018, paras 60-67

[31] As above, paras 137-138

[32] As above, para 136

[33] As above, paras 130-135

[34] Consolidation of defined benefit schemes, Department for Work and Pensions, 7 December 2018, paras 124-129

3.2 Interim regulation

A Pension Schemes Bill (now the Pension Schemes Act 2021) was introduced in the House of Lords in January 2020 without provisions for superfunds. At that point two superfunds, Clara and the Pensions Superfund, had been established, though neither was yet active.[35]

> During the passage of the Bill, the Minister for Pensions and Financial Inclusion Guy Opperman MP said that the "Government must bring forward legislation in respect of superfunds in the fullness of time". The Minister explained that the complexity of the required legislation will take time: I have looked at the process for superfund legislation, and it is definitely complex. We will have to respond to the present consultation, having considered the interim regime, and I know that superfund legislation will require at least a 50-clause Bill and probably close to a 100-clause Bill. Such legislation is not a simple undertaking; it will require a proper piece of parliamentary and statutory legislation that will take time.[36]

The Government is yet to respond to the consultation which closed on 1 February 2019.[37]

In the absence of legislation and with two potential superfunds having been established the Pensions Regulator undertook a "targeted consultation" looking at capital adequacy, value extraction and investments.[38] It said that it would take an interim approach to superfunds until there is a legislative regime.[39] This approach would follow two principles:

- A high degree of certainty that members' benefits would be paid in full.
- An approach reflecting the direction of travel of future legislation, influenced by the 2018 Government proposals.[40]

35 DB superfunds consultation response, the Pensions Regulator, 18 June 2020, para 2.6
36 Pension Schemes Bill Deb 5 November 2020 c120-121
37 Consolidation of defined benefit schemes, Department for Work and Pensions, 7 December 2018
38 DB superfunds consultation response, the Pensions Regulator, 18 June 2020, para 2.6
39 As above, para 2.1
40 As above, para 3.3

4 Current assessment process for superfunds

In June 2020 the Pensions Regulator published guidance for DB superfunds, following the response to its consultation.

Superfunds are expected to complete an assessment process with the Pensions Regulator before they can accept the transfer of a scheme. Although there was no specific legislative authorisation framework for superfunds, the Pensions Regulator explained that it could use its existing powers if funding, personnel or governance of a superfund was not fit for purpose. Section 7 of the Pensions Act 1995 gives the Pensions Regulator powers to remove and appoint a pension scheme's trustees if they are satisfied it is necessary to do so and Section 231 of the Pensions Act 2004 gives the Regulator powers relating to a scheme's funding.

The Pensions Regulator assesses superfunds against four key expectations:

- People
- Governance
- Systems and processes
- financial sustainability mechanisms and processes in respect of business plans, costs, assets and liquidity plan, investment governance and risk management[41]

The first superfund, Clara-Pensions, completed its assessment process in November 2021.[42]

The regulator has also published detailed guidance for trustees and sponsoring employers considering moving a scheme to a DB superfund.[43]

Superfund transactions

Sponsoring employers looking to transfer a scheme to a superfund are expected to receive clearance from the Pensions Regulator.[44] Superfunds should not accept schemes with the ability to buy-out, which is consistent

41 DB superfunds consultation response, the Pensions Regulator, 18 June 2020

42 DB superfunds list and assessment, the Pensions Regulator, 30 November 2021

43 Superfund guidance for prospective ceding trustees and employers, the Pensions Regulator, 21 October 2020

44 As above

with the proposals in the Department for Work and Pensions 2018 consultation.[45]

Financial sustainability and capital adequacy

During the interim period before legislation the Pensions Regulator aims "to ensure a high degree of certainty that members' benefits will be paid."[46] It expects superfunds to have detailed and costed plans for all likely scenarios include the fund winding up.[47]

The Pensions Regulator's capital requirements have been guided by the 99% probability of success in the Department for Work and Pensions 2018 consultation.[48] The superfund must choose prudent assumptions when measuring its liabilities.[49] The Pensions Regulator has set out the assumptions to be used for calculating a minimum level of funding known as minimum technical provisions.[50]

The capital buffer should be risk-based and include market and longevity risks. The market risk element is required to be at a level that there is a 99% probability of being funded at the minimum technical provisions or above in five years' time.[51]

The superfund must also include two legally enforceable triggers which result in action being taken if the scheme's funding level deteriorates. These are:

- **A low risk funding trigger**: If the scheme is funded below the minimum technical provisions level funds in the capital buffer are added to the pension scheme.
- **Wind-up trigger**: Set at 105% of the amount required to secure the benefits paid by the PPF with an insurer.[52] This amount is known as a section 179 valuation (s179) and set out in the Pensions Act 2004.[53]

Profits and fees

During the initial period superfunds will not be able to make a profit, unless member benefits are bought out in full with an insurer. If a legislation is not in place, the Pensions Regulator will review its decision within three years (by June 2023).[54]

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45 DB superfunds guidance, the Pensions Regulator, June 2020
46 Consolidation of defined benefit schemes, Department for Work and Pensions, 7 December 2018
47 DB superfunds guidance, the Pensions Regulator, June 2020
48 As above
49 As above
50 As above, Appendix A
51 As above
52 As above
53 Pensions Act 2004, s179
54 DB superfunds guidance, the Pensions Regulator, June 2020

Superfunds are permitted to apply fees and charges to pension schemes and the Pensions Regulator will “not be setting prescriptive limits” on how these are applied. These should, however, be no higher than equivalent market prices and disclosed to all parties before a scheme transfers to a superfund.[55]

55 DB superfunds guidance, the Pensions Regulator, June 2020

5 Comment and debate

5.1 Regulation

The Pensions Regulator regulates trust-based pension schemes. It is responsible for the interim regime and the consultations have proposed it would retain this role.

In July 2018, the Minister for Pensions and Financial Inclusion told the Work and Pensions Committee that consolidators will not be "operating in some sort of regulatory vacuum".[56] The Government's December 2018 consultation, Consolidation of defined benefit pension schemes, noted that:

> We consider that the current legislative framework does not prevent a superfund setting up and attempting to attract other funds to consolidate. However, there are clear risks in doing so without a suitable regulatory framework to ensure member protection.[57]

The Government's consultation proposed that most regulation for defined benefit consolidators will be undertaken by the Pensions Regulator, as is the case for other trust based occupational pension schemes.[58] The Government's consultation identified that superfundshave additional risks above and beyond traditional defined benefit schemes including:

- there is no enforceable recourse to the former employer
- the expectation of investors to make reasonable profits from the capital buffer
- the concentration risk from the multiple consolidated schemes using a single investment strategy[59]

There have been calls, notably from the Association of British Insurers, for superfunds to be regulated by either the Financial Conduct Authority, which regulates UK financial service firms and markets, or the Prudential Regulation Authority, which regulates insurers alongside other bodies such as banks. In response to the Department for Work and Pensions consultation on defined benefit pension schemes, the Association of British Insurer's said in February 2019:

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56 Work and Pensions Committee, oral evidence: Defined benefit pensions white paper, HC 956, 18 July 2018, Q241

57 Consolidation of defined benefit schemes, Department for Work and Pensions, 7 December 2018, para 12

58 As above, para 27

59 As above, para 22

> … commercial consolidators will be profit-seeking institutions, similar to investment banks, hedge funds and insurers, rather than DB pension schemes which are not-for profit and run under trust law. Financial institutions are regulated by the FCA and the PRA for purposes of conduct and capital. These regulatory regimes give the PRA and the FCA robust authorisation, rule-making and supervisory powers. Such powers will be necessary for the regulator of commercial consolidators. A principles-based code of practice as proposed is not a suitable regulatory tool for profit seeking institutions responsible for potentially hundreds of billions of pounds of savers' pension entitlements. It is obvious that the appropriate regulators for commercial consolidators are the PRA and the FCA.[60]

Although the introduction of superfunds does not materially change the size of the funds regulated by the Pensions Regulator, the level of regulation likely to be required is more substantial than under current arrangements. Charles Counsell, CEO of the Pensions Regulator, told the Work and Pensions Committee in June 2019:

> If one (a superfund) came into existence tomorrow or next week with a scheme that was part of the superfund, it would be based on a voluntary regulation process. I don't think that is the best place for us to be. I do believe that we need proper regulation of superfunds to be in place. Again, this is another matter for the Pensions Bill for later this year.[61]

5.2 Pension Protection Fund levy

The PPF is the statutory fund to protect members of defined benefit pension schemes if their scheme becomes insolvent. The PPF is funded by levies on all eligible DB schemes. The majority of the levy is raised on a risk-based approach. The greater the probability of a sponsoring employer becoming insolvent and leaving the scheme funded below PPF levels the greater the levy.[62]

In evidence submitted to the Work and Pensions Committee in 2018 the PPF said:

> If superfunds are eligible for PPF protection we will be exposed to the risk of failure in their investment strategy. This is unlike the current situation with schemes where the employer provides the first line of defence. While we expect superfunds to pursue relatively low risk investment strategies, this will not entirely remove the risk of investment failure. Given the potential size of a superfund, deficits could become very substantial in real terms before the superfund initiates a claim on the PPF. A particular concern is that we expect

60 The ABI's response to the Department for Work and Pensions consultation on Consolidation of Defined Benefit pension schemes (PDF), Association of British Insurers, February 2019

61 Work and Pensions Committee, Oral evidence: The work of the Pensions Regulator, HC 2092, 26 June 2019, Q63

62 Policy statement, Levy rules 2022/23, Pension Protection Fund, 16 December 2021

> each superfund might invest in a similar way, meaning that, if one superfund collapses, others could also do so at the same time.[63]

The PPF also stated that an effective regulatory regime for superfunds must achieve the four aims below:

> 1. Protect members and PPF levy payers from the potentially significant impact of 'superfund' failure,
>
> 2. Prevent superfunds from proceeding unless they are financially robust and provide a high degree of confidence that scheme benefits will be paid in full,
>
> 3. Ensure any transfer into a superfund from a scheme is a move that provides greater security for the scheme members,
>
> 4. Ensure any sale of a superfund doesn't increase the risk to members or the PPF.[64]

The Pension Protection Fund published alternative covenant scheme guidance for the 2022/23 levy year which it says will be of particular assistance to superfunds.[65]

5.3 Superfunds as an alternative to buy-out

Transferring to a superfund is expected to be cheaper than securing full buy-out with an insurer. There is a perceived risk of superfunds being used for regulatory arbitrage, by avoiding the same requirements as an insurance provider. In its December 2018 consultation the Government stated that:

> Superfunds have some similarities to insurance, given that the traditional employer link is broken, and the protection for members' benefits in the long term is provided by a capital buffer. ... Superfunds will not be required to provide the same level of confidence that benefits will be paid in full as an insurer following a buy-out of the scheme liabilities.[66]

And that:

> A strong regulatory framework for superfunds will be needed to ensure that there are appropriate protections for members and that the risk of regulatory arbitrage with the insurance buy-out market is minimised. Without an effective gateway superfunds would enjoy a considerable competitive advantage in the

63 Work and Pensions Committee, Defined benefit pensions white paper inquiry, Pension Protection Fund – written evidence, BPW0029, 23 May 2018

64 As above

65 Alternative Covenant Scheme Guidance 2022/23 Levy Year, Pension Protection Fund, December 2021, para 1.2

66 Consolidation of defined benefit schemes, Department for Work and Pensions, 7 December 2018, para 18

> price of acquiring DB schemes compared to insurers given the lower capital requirements in the occupational pension space.[67]

Responding to the Government's consultation, the Association of British Insurers said that the proposals "only help employers to walk away from their obligations to their employees on the cheap, rather than addressing the need to help under-funded schemes".[68] Yvonne Braun, Director of Policy, Long-term Savings and Protection, ABI, told the Work and Pensions Committee that:

> The prices for buyouts, as has been talked about, are prohibitively expensive. That reflects a very robust regime put in place by Solvency II, the European regulation, and the Prudential Regulation Authority here, part of the Bank of England, and that reflects ultimately that member benefits are paramount. …
>
> That sort of robust regulation is what I would contrast with what is being proposed here, because ultimately what we are talking about is employers being able to walk away from their pension promise. … It is also being proposed that should be regulated by The Pensions Regulator. I think it is fair to say that they have very little expertise of regulating for-profit pension entities. They now have a system in place for a master trust, which is essentially brand new, and untested. Otherwise, they are not used to regulating for-profit entities. That is what the Bank of England, the PRA, do.[69]

5.4 Regulation before a legislative authorisation framework is in force

Under current legislation, superfunds are treated the same as other trust-based DB schemes.[70] The Pension Regulator said that it would take an interim approach to superfunds until there is a legislative regime.[71] The Pensions Regulator had said it anticipated legislation being introduced in 2022-23 but has more recently said that it will "continue to work with government to consider a legislative solution in the longer term."[72]

Although there was no specific legislative authorisation framework for superfunds, the Pensions Regulator explained that it could use its existing powers if funding, personnel or governance of a superfund was not fit for purpose. Section 7 of the Pensions Act 1995 gives the Pensions Regulator powers to remove and appoint a pension scheme's trustees if they are

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67 As above, para 19
68 As above
69 Work and Pensions Committee, oral evidence: Defined benefit pensions white paper, HC 956, 6 June 2018, Q118
70 Consolidation of defined benefit schemes, Department for Work and Pensions, 7 December 2018, para 12
71 As above, para 2.1
72 Corporate Plan 2021-24, The Pensions Regulator, 19 May 2021 and Corporate Plan 2022-24, The Pensions Regulator, 13 June 2022

satisfied it is necessary to do so and Section 231 of the Pensions Act 2004 gives the Regulator powers relating to a scheme's funding.

The Association of British Insurers said that the interim regime "is no replacement for legislation" and that:

> Trustees of schemes have one shot at severing the employee covenant, so they need to get it right and ensure scheme members are front and centre of any decision. As it stands the guidance is part of a regulatory regime which is not strong enough; legislation is needed as soon as possible.[73]

The Chair of the Pensions Regulator told the Work and Pensions Committee that until legislation "it remains a voluntary regime so it may be difficult to exercise our authority if there are individuals or entities that seek to not work with us on the protection of savers."[74]

73 ABI responds to The Pension Regulator's guidance for trustees considering transferring to a superfund, Association of British Insurers, 21 October 2020

74 Work and Pensions Committee, Appointment of the Chair of the Pensions Regulator, 21 April 2021, Q27

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