Superfunds
Learning Manual

Clara
PENSIONS

Introduction

Commercial consolidators or “superfunds” first started to gain traction in 2018 when the Department for Work and Pensions published a white paper identifying opportunities to provide positive outcomes for defined benefit schemes that couldn’t afford an insured buy-out. Two years later guidance was published by The Pensions Regulator (TPR) on how these superfunds should be operated, and three years after that, Clara-Pensions completed the first Superfund transactions with the Sears Retail Pension Scheme and the Debenhams Retirement Scheme.

Today, with more and more defined benefit schemes considering their “endgame” approach, superfunds are becoming an increasingly looked at option for trustees and sponsors. While a superfund might not be the right choice for every scheme, understanding the role and mechanics of how they work is vital to make the best choice on behalf of scheme members and their benefits.

This briefing explains what superfunds are, how they function, how a transfer to a superfund works, and why they are becoming an essential consideration for schemes.

What is a superfund?

A pension superfund, also known as a commercial consolidator, is an entity designed to consolidate and manage the liabilities of multiple defined benefit (DB) pension schemes under one umbrella. There are different models and 'flavours' of superfund either in operation or that have been proposed, but all of them operate a UK pension scheme into which other schemes transfer their members and corresponding assets and liabilities to. At the time of writing, Clara-Pensions is the UK's only superfund that has completed TPR's assessment and therefore is able to transact.

The primary goals of a superfund are to improve member outcomes and increase member security. Their focus is on schemes who cannot access buy-out with an insurance company (for example, sponsors who want to de-risk their pension fund but don't have the funds to access buy-out, trustees of schemes with weak sponsors who want to secure their members' benefits, or schemes in PPF assessment whose members would be better off in a superfund than under an insurance regime). Superfunds achieve their goals by:

a. Injecting additional, external capital to act as a 'buffer' fund that enhances security and further protects members' benefits from underfunding risks.

b. Taking advantage of pooled expertise and economies of scale. Larger schemes typically benefit from reduced investment or administration costs per member, which makes superfunds attractive to many schemes. Larger asset pools also allow for more sophisticated and diversified investment strategies, potentially improving long-term returns and improving diversification risk. Expertise that usually would only be accessible to larger schemes, such as sophisticated risk management functions and governance structures can be shared between smaller schemes, potentially meaning risks are managed more effectively.

As commercial entities, superfunds also seek to provide a return to their capital providers, however there are strict rules governing how and when this is done in order to protect members. A superfund will usually return capital and investment or residual proceeds once members benefits are deemed to be sufficiently secure, in line with strict TPR requirements. This could be following a full buy-out with an insurer, or once funding levels have increased above a given threshold.

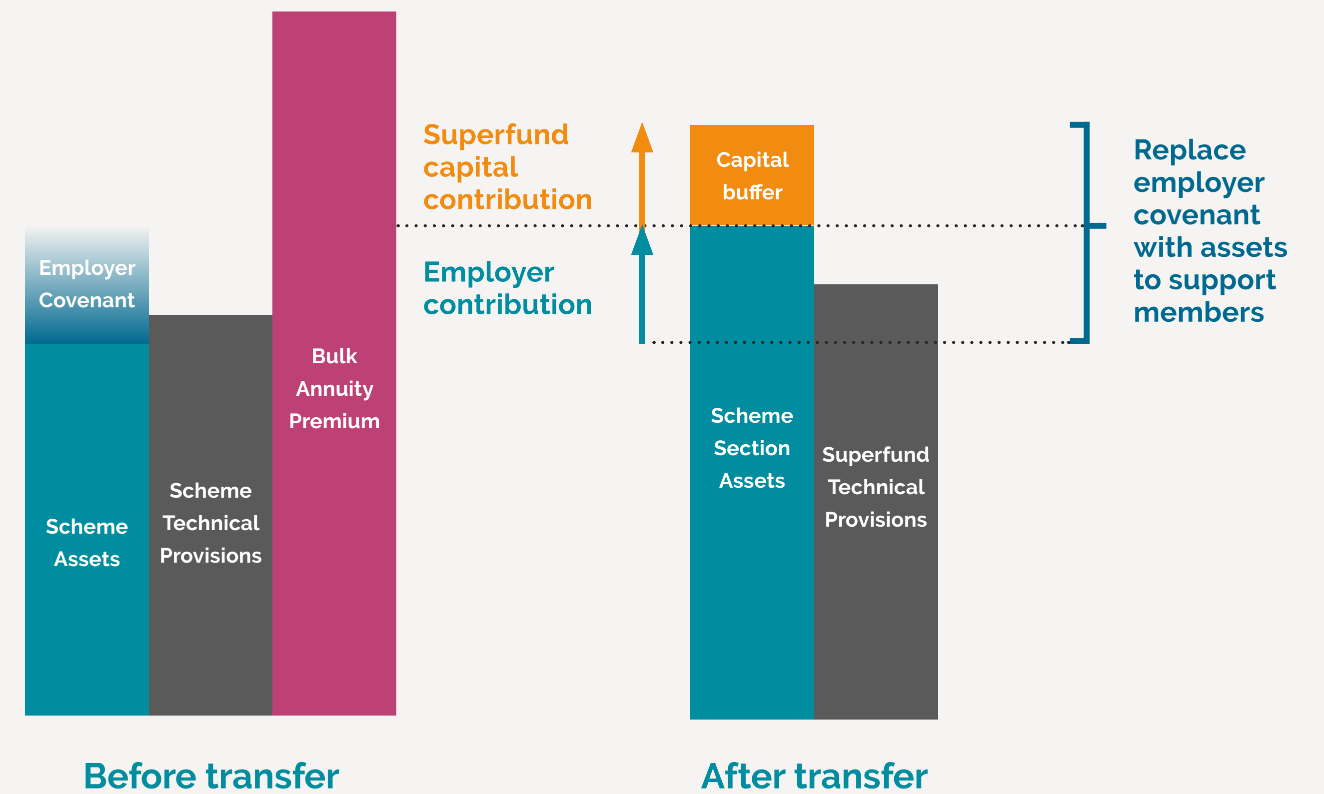
Key features of superfunds:

- **TPR regulated UK DB schemes:** superfunds allow pension schemes to transfer their liabilities to the consolidator's scheme. This involves members from the ceding scheme transferring via bulk transfer to the consolidator's pension scheme, which will be a UK registered pension scheme. The consolidator's scheme may be segregated, with each scheme joining a separate section, or it could be pooled. This depends on the design of the consolidator and its model.
- **Regulatory oversight:** Superfunds in the UK are subject to oversight by TPR, which has established guidelines to ensure that these entities operate with appropriate financial security and governance. TPR's interim regulatory framework, introduced in 2020 and updated in 2023 and 2024, sets out the conditions under which superfunds must operate, with a particular focus on ensuring that pension member benefits are safeguarded to a very high degree. Any superfund wishing to take on members must first undergo a rigorous assessment process with TPR before it is given the green light to do so.
- **Buffer assets:** A superfund's assets will be made up of assets from the ceding scheme (which may be paid as cash or transferred in-specie), additional capital provided by the superfund, and in some cases a top-up from the ceding scheme's employer as well.
- **De-risking alternative to buy-outs:** Superfunds provide an alternative to a traditional buy-out with an insurance company, which is often too expensive for many underfunded schemes. A buy-out involves transferring the pension scheme's liabilities to an insurer, who guarantees the payment of benefits in exchange for a premium. Superfunds offer a similar solution but with different pricing structures and regulation, making them a viable option for schemes that cannot afford or access a full buy-out. Under some superfund models (like Clara-Pensions), the superfund acts as a 'bridge' for schemes, enabling them to reach buy-out in due course.

How do superfunds work? The regulatory landscape and transferring into a superfund.

Regulation

UK legislation for pension superfunds does not yet exist but is expected to be introduced as part of broader pension reforms. In the 2024 King's Speech, the government reaffirmed its commitment to consolidating the Defined Benefit (DB) pension market, with a focus on establishing a permanent legislative framework for commercial superfunds. The legislation will clarify the rules around superfunds, ensuring they meet rigorous funding requirements and maintain a high probability of paying pension benefits in full. This is part of a wider effort to improve the sustainability of DB pension schemes, with draft legislation anticipated to be in place by 2026.



In the meantime, superfunds operate within guidance issued by TPR. This guidance is regularly reviewed and updated and seeks to ensure that superfunds:

- **Are managed by people with the required expertise, adhering to rules set by TPR on governance and processes.**
- **Are only used by trustees and sponsors when they are in members' best interests through the application of the 'Gateway Test'.** Each transfer is individually assessed and if there is a realistic prospect of insurance buy-out now or in the foreseeable future then a transfer will not be allowed. TPR also reviews these transfers.
- **Have enough assets at the outset to protect from key risks pension schemes face and adhere to minimum capital requirements.** These requirements specify that a scheme must have enough assets to protect against market, longevity and any other material risks in 99% of scenarios over a 5-year time horizon. These assets are usually 10%-20% higher than a prudent measure of a scheme's liabilities, and so the superfund will contribute some of this requirement.
- **Ongoing monitoring and intervention triggers.** Superfunds must monitor funding levels against two 'triggers' on a quarterly basis: the low-risk trigger (100% of Technical Provisions) and the wind-up trigger (105% of the Pension Protection Fund's Section 179 basis). If these are breached actions will be taken to ensure members' benefits are protected.

TPR's interim regime for superfunds was most recently updated in August 2024 and is designed to reflect the government's stated direction of travel for superfund legislation.

Transferring a scheme

In exchange for taking on the liabilities of the ceding scheme, the superfund will charge the ceding scheme a premium in a similar manner to an insurer during a buy-out. This premium will be based on the size and shape of the scheme's liabilities and will be used to make up part of the scheme's capital requirements. The remainder will then be provided by the superfund. Typically, superfund premiums are lower than insurance premiums due to the different regulatory regimes.

As part of a transfer, the ceding scheme exchanges its sponsor covenant for the additional capital provided by the superfund and/or the sponsor. In making a decision to transfer to a superfund, trustees must decide whether this is a suitable exchange.

The superfund premium may be paid using cash or could involve an in-specie transfer of assets from the ceding scheme. This can help schemes avoid needing to sell certain assets such as illiquids at short notice and facing the increased costs and reduction in sale proceeds of doing so. Superfunds are able to accept a wider range of assets than insurers due to the difference in rules that apply to UK pension funds and insurers.

Benefits of Superfunds

Trustees

A superfund trust will be managed by a trustee, or trustee board. Members of the Clara Pension Trust for example are looked after by an experienced board of professional trustees whose sole focus is to act in the best interests of members. This includes, but is not limited to, day to day management of the trust, monitoring funding levels and investments, appointing and reviewing service providers and their service quality, engaging and informing members, and making decisions on any discretionary benefits which may be due.

A superfund trust will be managed by a trustee, or trustee board. Members of the Clara Pension Trust for example are looked after by an experienced board of professional trustees whose sole focus is to act in the best interests of members. This includes, but is not limited to, day to day management of the trust, monitoring funding levels and investments, appointing and reviewing service providers and their service quality, engaging and informing members, and making decisions on any discretionary benefits which may be due.

Unlike traditional sponsors, who may juggle various corporate responsibilities, superfunds are solely focused on the consolidator's scheme, ensuring members experience an appropriate level of service and regular communication, as well as overseeing the scheme from a risk and governance point of view.

If the superfund operates the 'bridge' model to a future insured buy-out, then the trustees will also focus on preparing members for that future. Members benefit from a clear understanding of the timeline and processes involved in this, leading to greater peace of mind.

This specialised focus also mitigates potential conflicts of interest that can arise when a sponsoring employer may become distracted by other corporate needs. As a result, members have greater confidence that the security of their pensions are of top priority and are managed by qualified and experienced trustees.

Scheme Partners

Consolidating schemes into a superfund can also enhance the bargaining power of the superfund when negotiating with service providers, ensuring they receive better value for money and the best possible outcomes.

As with many insurers and pension schemes, superfunds typically have access to experienced scheme and business partners, including expert pension administrators and investment managers. This is crucial for members as it allows for the selection of the best suited administrators who are dedicated to providing members with excellent service.

Superfunds are regulated by TPR and are obliged to provide regular, detailed and transparent reporting. This not only includes the funding levels of the sections, but also the member experience (such as service levels, complaints and member engagement) which is closely and regularly monitored.

Funding & Investment

Another significant advantage of superfunds is the immediate additional funding provided by their capital backers. They recognise the potential of consolidating pension liabilities within a superfund structure and are willing to inject capital to immediately increase the schemes funding level, and therefore increase the security of members' benefits, ensuring that members receive their promised benefits without delay.

Summary

DB superfunds provide many benefits to scheme members, including cost efficiencies through consolidation, access to top-tier administrative expertise, immediate, additional funding from their capital backers, and in the case of the 'bridge to buy-out' model a focused approach to preparing for insurance buy-outs.

When transferring to a superfund, members are welcomed to a community which aims to provide transparent communication and excellent service whilst preparing the section for buy-out. By eliminating distractions and conflicts of interest common in traditional sponsorship models, superfunds can enhance the security and management of pension schemes, ultimately leading to better outcomes for members.

What schemes are suitable for consolidation?

Superfunds are designed to help schemes that cannot access buyout due to affordability or other structural (illiquid assets, data etc.) issues. This is ensured by TPR's gateway test which doesn't allow the transfer of any scheme that can pursue an insurance endgame in the short term. While not every scheme will be able to afford to access a superfund yet, their creation enables far more schemes to benefit from additional security than was possible before their creation.

Schemes that are currently most suitable for superfunds generally have the following characteristics.

Funding Level

Superfunds are required to allocate enough capital to a scheme to ensure that they have enough assets to protect members' benefits in line with TPR requirements.

They also need to produce acceptable returns for their capital providers, which puts a limit on the minimum value of assets required to make the transaction viable.

Schemes therefore need to have a funding level in a sweet spot. This is typically less than fully funded on a buy-out basis, but able to afford the superfund premium or have a sponsor that can top-up the scheme to the required level.

Maturity

Generally, superfund premiums are lower for schemes with a deferred-heavy population, and pricing is more attractive for less mature schemes.

Employer Covenant

Schemes with a very strong sponsor covenant are unlikely to benefit materially from the security that superfund capital provides. Stronger sponsors of schemes which are not yet able to access insurance can unlock business value by removing the obligations and risks associated with their pension scheme from the corporate balance sheet. This type of project can finance itself if some of the value created is used to pay the superfund transfer premium.

Schemes with funding levels relatively close to insured buy-out but with a weak sponsor covenant can speed up the journey to that buy-out and reduce the likelihood of negative member outcomes in the meantime.

In circumstances where a sponsor has failed and its scheme has exited the PPF assessment process, the trustees will look to secure members' benefits. Here a superfund transaction can offer the possibility of securing member benefits in full in the event scheme assets are not sufficient to secure 100% of benefits with an insurer.

Preparing a Pension Scheme for a superfund

Pension scheme managers and trustees play a crucial role in preparing their schemes for a superfund or buy-out transaction. These transactions—whether transferring liabilities to a superfund or securing benefits through a buy-out with an insurer require careful planning and proactive decision-making. Here we outline some steps that pension trustees and scheme managers can take to ensure a successful process.

Understanding Scheme Readiness

Managers should evaluate the readiness of the pension scheme for a superfund transfer.

This includes an assessment of the scheme's funding position. Ideally a scheme should already be able to demonstrate that they are not able to afford an insurance solution in the short term. By approaching the insurance market ahead of engaging with consolidators, it avoids needing to do this prior to a transfer, should evidence be needed.

Setting up appropriate governance frameworks, involving key decision makers both the scheme trustee board and the sponsor can speed up the process, avoiding delays which increase execution risk.

Depending on the current scheme administration, a superfund may request a transfer of administrator to (one of) their preferred provider(s). This will form a part of the commercial negotiation process as if long-term agreements have been made with incumbent service providers, then the trustees should consider what the best approach is.

Data quality, Cleansing and legal review of benefit specifications.

Most superfund transfers are more akin to a full insurance buy-out, without a data cleanse period and corresponding true-up. This means that superfunds need to be more certain of the liabilities they are agreeing to take on than an insurer might be, given that there is less recourse to make up any shortfall in light of further data and benefit auditing.

Particular areas which may need further consideration are dependant data (such as marital status and date of births, and postcodes), which may not be held by the scheme currently but would be expected to be obtained prior to seeking superfund pricing.

With this in mind, trustees should check that their data is high-quality and accurate. In addition, it's important that the benefit specifications are legally reviewed to ensure that the benefits described are consistent with the trust deed and rules, as well as past trustee discretionary practices, equalisation rules and legislation. This includes reviewing aspects such as discretionary benefits and codifying these, inflation protections, and anyany complex member entitlements.

Considering member communications

Trustees must carefully consider how to communicate with pension scheme members when preparing for a superfund or buy-out transaction. For a superfund, members may need reassurance about the new structure and how it impacts long-term security, as superfunds are a relatively new concept compared to traditional insurance buy-outs.

Member experience will likely change slightly following transfer to a superfund. This may be through accessing information in different ways, such as via different portals or websites, especially if administration providers have changed.
Ahead of any transfer, trustees should provide clear, transparent information about the transfer, the protections in place, and any changes to member options.

Reviewing and Structuring Scheme Assets

Trustees must also consider the structure and quality of the scheme's assets. They should evaluate how easily those assets can be liquidated or transferred, particularly if a transfer is needed to take place imminently. Superfunds have more flexibility than insurers, but they may not place the same value on certain assets as a ceding set of trustees.

If the scheme holds illiquid assets, such as property or private equity, trustees may need to plan for their sale or restructuring to align with the needs of the insurer or superfund.

Disclaimer

No member of the Clara group nor any related or affiliated party (including, without limitation, any direct or indirect investors in the Clara group) (such related or affiliated parties being "Affiliates") makes any representation or warranty, express or implied, as to the adequacy, accuracy, reliability or completeness of any information provided in this document (the "Information"), or as to the reasonableness of any forecasts or assumptions on which any of it is based.

No member of the Clara group, nor any of its Affiliates, professional advisers or service providers, have any liability resulting from the use of the Information. In making the Information available, no member of the Clara group (nor any of its Affiliates) accepts any responsibility or liability (whether express or implied) to provide any advice, or to update or correct any inaccuracies which may become apparent in any of the Information. For the avoidance of doubt, parties dealing with the Clara group are responsible for taking their own independent legal, tax, financial, actuarial and/or investment advice in relation to the Information.

The Information does not comprise or contain any invitation or inducement to engage in any form of investment activity but, in any event (and subject always to the terms of any applicable confidentiality undertakings), it is only directed at (and must only be viewed by):

a. persons of the kind described in articles 19 and 49 (2) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005; or
b. any other persons to whom the Information may be lawfully communicated.

Distribution of the Information by the Clara group is intended to be restricted to the UK. Anyone who receives the Information must also observe that restriction or ensure compliance with all legal and regulatory requirements in any other relevant jurisdiction.

Authors

Louise Ellisdon
Client Relationship Manager,
Clara-Pensions

Sam Tomes
Senior Pricing Actuary,
Clara-Pensions

Matt Wilmington
Chief Transactions Officer,
Clara-Pensions

For more information, please visit: **clara-pensions.com**

Registered Office:
6th Floor
9 Appold Street
London EC2A 2AP

T: +44 (0) 20 7247 1452

E: pmiqualifications@pensions-pmi.org.uk

pensions-pmi.org.uk

Clara
PENSIONS