HYMANS ROBERTSON

BRIEFING NOTE

DB funding code: routes to compliance

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The Pension Regulator's (TPR's) new funding code for DB schemes will apply to valuations after 22 September 2024, so you need to start preparing now.

To decide whether your strategy is more suited to the Fast Track or Bespoke route, you can use our updated interactive tool, which also lets you test what would happen if you had a change in funding or strategy.

Two routes to compliance:

Bespoke

- Scheme-specific flexibility
- Puts an onus on trustees to explain and show how risk is supported
- More regulatory scrutiny than Fast Track

Fast Track

- TPR's tolerable level of risk in normal circumstances
- TPR unlikely to scrutinise a valuation if the scheme actuary confirms that it passes three tests
- TPR can focus its limited resources on schemes taking the Bespoke route

Fast Track Test 1: technical provisions

Technical provisions must be a **minimum proportion of liabilities** measured on a low-dependency basis that uses a discount rate of gilts + 0.5%, increasing as the scheme matures.

- 85% at 20 years' duration
- 96% at 15 years' duration
- Equal to the low-dependency liabilities at significant maturity (10 years' duration)

Fast Track Test 2: recovery plan

The recovery period must be **no more than six years** for a scheme not yet at significant maturity, or three years for a significantly mature scheme.

- No investment outperformance allowed
- No back-loading (CPI or fixed 3% p.a. increases only)
- Look at afforability year by year
- The scheme can take account of post-valuation experience

Fast Track Test 3: investment stress

The scheme's funding position must fall by **less than the maximum risk parameter** under the PPF's tier 1 stress test (broadly a one-year 1-in-6 value-at-risk (VaR) event).

- 13.1% at 20 years' duration
- Tapers to 2.2% at significant maturity
- For immature schemes, TPR suggests this implies around 60% growth assets, with the rest in credit and LDI (2x leveraged), de-risking to 15% growth assets

The code also requires the scheme's assets to be liquid enough that the scheme can meet expected cash flow requirements and make reasonable allowance for unexpected cash flow requirements.

Low-dependency objective

To be eligible for Fast Track, a scheme must **pass all three tests** and **set a low-dependency objective** for significant maturity.

Significant maturity is the point at which a scheme reaches a duration of 10 years on the low-dependency basis. Open schemes can allow for up to nine years of future accrual or new entrants. The scheme actuary is responsible for estimating the date of significant maturity.

Maximum supportable risk

For all schemes, the **employer covenant** must be able to support a stress scenario. Trustees expected to carry out analysis to satisfy themselves that the scheme could recover from a downside scenario (one-year 1-in-6 VaR event suggested). A stronger covenant can support more investment risk.

The **covenant reliability period** is the period over which there is reasonable certainty over employer cashflows (typically expected to be around three to six years). The stress must be supportable by the employer's affordability over this period.

Is Fast Track right for your scheme?

Fast Track is not optimal for all schemes. TPR has still to set out in detail how it will regulate Bespoke, but the central concept for all schemes is that they must be able to support risks to funding.

To prepare for the code, check whether your scheme is eligible for Fast Track. Our updated interactive tool can help you quickly identify whether your current strategy is more suited to the Fast Track or Bespoke route. You can also use it to test what would happen if you had a change in funding or strategy.

If your scheme is not eligible for Fast Track, consider whether you can 'repackage' your plans to meet the requirements.

Want to find out more?

To find out how we can help you prepare for the new funding code, please get in touch with your usual Hymans Robertson contact or one of our experts.

Laura McLaren
Partner and Actuary
0141 566 7914
laura.mclaren@hymans.co.uk

Stephen Jasinski
Senior Investment Consultant
0131 656 5134
stephen.jasinski@hymans.co.uk

Lauren Branney
Associate Actuarial Consultant
0121 212 8138
lauren.branney@hymans.co.uk

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