

## Pension Schemes Bill published: new Pensions Regulator powers

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The new Pension Schemes Bill published today would, if enacted, significantly bolster the Pensions Regulator's powers in relation to defined benefit pension schemes by introducing: new criminal offences, new civil penalties and changes to the current contribution notice regime. These could have major implications for corporate transactions and the management of defined benefit pensions liabilities. The Bill also introduces a number of other major changes (e.g. collective defined contribution schemes). We will be looking at these in a future publication.

### New criminal offences

The Bill would create two new criminal offences which can apply to **any person** (including individuals, e.g. directors, and regardless of whether the person has any connection to, or association with, the scheme or its employer):

- avoidance of employer debt to a defined benefit pension scheme, and
- conduct risking accrued defined benefit pension scheme benefits.

**Avoidance of employer debt** is defined as being any act or course of conduct which prevents the recovery of all or part of a Section 75 ("buy-out") debt, prevents such a debt becoming due, compromises or settles the debt or reduces the debt.

**Conduct risking accrued scheme benefits** is defined as being any act or course of conduct that *"detrimentally affects in a material way the likelihood of accrued scheme benefits being received"*.

For the first offence, the person must have intended that the act or course of conduct would prevent the recovery of the debt, prevent the debt becoming due etc.

For the second offence, the person must have known or ought to have known the act/conduct would have the detrimental effect.

In both cases, there is no offence where the person had a "reasonable excuse" for their actions.

**Sanctions:** Anyone found guilty of these offences faces up to **7 years' imprisonment** and/or **unlimited fines**.

### New civil penalties

The new civil penalties of up to £1 million can apply more broadly. Any person who was party to an act or failure to act with a main purpose of avoiding an employer debt or which risks accrued scheme benefits (both as defined above), where it was not reasonable for the person to act that way, can incur this penalty.

**Comment:** These offences and penalties replace the headline grabbing formulation of "wilful or reckless conduct in relation to a pension scheme" mentioned in the consultation leading up to the Bill. Points to note include that:

- the offences are very broad and would appear to catch actions routinely taken by defined benefit pension scheme sponsors and trustees to prevent section 75 debts arising, e.g. flexible apportionment arrangements,
- the penalties can apply to individuals, e.g. directors, as well as companies and regardless of whether the person being targeted has any connection to, or association with, the pension scheme or its employer, and
- there is no definition of “reasonable excuse”.

It remains to be seen whether, for a non-associated person, such as a bank advancing money to a defined benefit pension scheme employer under a secured facility, acting in their own commercial interests would be accepted as “reasonable excuse”. For example, in relation to the “conduct risking accrued scheme benefits” offence, while a competing creditor has no responsibility for delivering the pension scheme benefits, their actions could nevertheless have the effect the offence describes. Presumably, acting in an employer’s own commercial interests would not constitute “reasonable excuse”.

Whatever the position reached on what constitutes a “reasonable excuse”, we expect these new offences would make parties much more cautious when undertaking transactions involving entities with defined benefit pension schemes.

## Contribution notices

There are to be two new grounds for issuing a contribution notice:

- an employer insolvency test, and
- an employer resources test.

The “**employer insolvency test**” will allow the Pensions Regulator (“**tPR**”) to issue a contribution notice on a defined benefit pension scheme employer or any person connected to or associated with the employer (including individuals, e.g. directors) where, in tPR’s opinion:

- immediately after the act/failure to act to which the person was party, the pension scheme is in deficit on a Section 75 (“buy-out”) basis (using tPR estimates of scheme asset and liability values), and
- if a Section 75 debt had been triggered at the time, the act/failure to act would have **materially** reduced the amount of the debt likely to be recovered by the scheme.

The “**employer resources test**” will allow tPR to issue a contribution notice on a defined benefit pension scheme employer or any person connected to or associated with the employer (including individuals, e.g. directors) where, in tPR’s opinion:

- the person was party to an act/failure to act which reduced the value of the “resources” of the employer (what constitutes “resources” will be set out in regulations and they will be calculated and verified in a manner prescribed in regulations), and
- the reduction was **material** relative to the amount of the Section 75 (“buy-out”) debt, as estimated by tPR, which would have been triggered if the scheme had commenced winding-up at the time of the act/failure to act.

In both cases, defences are available if:

- the person gave due prior consideration (tested objectively) to the reduction in the hypothetical Section 75 debt recoveries or reduction in value of employer resources relative to the hypothetical Section 75 debt (as appropriate), and
- after taking any reasonable steps to eliminate or minimise that effect,

- it was reasonable in the circumstances to conclude that the act or failure to act did not have that effect.

There is a further defence for the “employer insolvency test” if it can be shown that, in fact, the scheme was not in deficit at the relevant time – it is assumed that this will also be on a Section 75 (“buy-out”) basis but the Bill does not yet make this clear.

The reasonableness test for imposing liability under a contribution notice is to be amended, as expected, to take into account the effect of the act or failure to act on the value of the scheme’s assets or liabilities. It is also amended to take account of a failure by an employer or connected or associated person to notify a notifiable event.

**Comment:** These changes to the contribution notice regime will considerably strengthen tPR’s powers when dealing with corporate transactions, in circumstances where pension schemes are not given due consideration. The defences to the new test will have to be carefully considered when assessing the risk of the use of moral hazard powers in future transactions and parties may be more likely to apply for formal clearance from tPR in future. One issue to note in particular is the potential difficulty of mitigating the impact of a corporate transaction on the resources of any employer. Where a defined benefit pension scheme employer sells a business and the proceeds are distributed to shareholders, providing a parent company guarantee or other security may well mitigate any potentially detrimental impact of the disposal on (i) the likelihood of scheme benefits being received or (ii) the scheme’s recoveries in an insolvency scenario. However, it would not seem to mitigate any impact on the employer’s resources. So, parties would be relying on the requirement for tPR to be of the opinion that it is reasonable to impose liability.

Slaughter and May (SZZM/CZXS/RSZH)

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