



# News Alert 2019/01

12 February 2019

## *Building a stronger Pensions Regulator – the Government responds*

### *At a glance*

**Amidst somewhat misleading publicity at the weekend about sending directors to jail for wilful and reckless behaviour in relation to a pension scheme, on Monday the Government responded to its June 2018 consultation on strengthening the Pensions Regulator's powers. This response has sifted some of the wheat from the chaff, but there remains much to be done before there is clarity on the new regime.**

### *The Detail*

On 11 February 2019 the Department for Work and Pensions [responded](#) to its consultation from last June that was concerned with protecting DB pension schemes by strengthening the Pensions Regulator's powers (see our [News Alert](#) issued then). Much of what was proposed is to go ahead, although the Government has rowed back on some proposals and a great deal of important detail on what is to go ahead has yet to emerge.

This News Alert looks at how the Government's proposals have changed and what is likely to happen next.

### **Corporate transaction oversight**

One of the most significant aspects of the DWP's consultation was a set of proposals through which the Pensions Regulator would obtain a greater insight into corporate transactions with the potential to do harm to DB schemes.

### **Notifiable events**

Four employer-related event additions to the notifiable events framework had been proposed, but now only two are to go ahead – namely:

- sale of a material proportion of the business or assets of a scheme employer which has funding responsibility for at least 20% of the DB scheme's liabilities; and
- granting of security on a debt to give it priority over debt to the DB scheme.

In response to concerns about the definition of terms relating to these two, the DWP promises to engage with stakeholders to develop its thinking further – and will subsequently consult on draft regulations to amend the framework.

The two which have been dropped, following concerns about their practicability, are:

- significant restructuring of the employer’s board of directors and certain senior management appointments; and
- the sponsoring employer taking independent pre-appointment insolvency/restructuring advice (such as an independent business review).

The DWP had also proposed removing the “wrongful trading of the sponsoring employer” notifiable event and extending the “breach of banking covenant” notifiable event. The former is to go ahead but the latter will not – again on practicability grounds.

The DWP has confirmed that it does not propose to extend the framework to cover the payment of dividends, or anything else at this stage. However, it does note that the Pensions Regulator will consider the level of dividend payments made when looking at scheme funding issues.

It is not clear whether the DWP is to go ahead with bringing forward the timing of notification of three employer-related events – namely the sale of the controlling interest in a sponsoring employer, the sale of the business or assets of a sponsoring employer, and the granting of security in priority to scheme debt. This is because the DWP recognises that there is more work to be done before it can establish where earlier notification could be beneficial and assuming it does whether it should be expressed in legislation or guidance. The DWP promises to work on this with the Pensions Regulator and the pensions industry.

In addition, consultation is promised on possible changes to scheme-related notifiable events and those arising from the separate consultation on the consolidation of DB schemes. The Pensions Regulator is to update its guidance on the notifiable events framework and consult on a revised Code of Practice which is to extend to the declaration of intent (see below).

### *Our viewpoint*

*These appear to be sensible changes of tack in the light of consultation responses, but with the core intentions undisturbed. But scheme sponsors are likely to be concerned at the continuing lack of detail as to the circumstances in which the two new notifiable events will operate, as well as the uncertainty as to whether the accelerated reporting in relation to three notifiable events will go ahead – and if it does, precisely how it will operate.*

**Declaration of Intent**

The DWP is to go ahead with the proposed new corporate declaration of intent to follow the three employer-related notifiable events whose timing may be brought forward (see above). It seems that as proposed, this employer’s declaration must set out the implications of the transaction for the DB scheme and how any risks will be mitigated. However, consultation is promised on the content of the statement.

The DWP also recognises that more work needs to be done on when the declaration should be shared with the trustees and the Pensions Regulator. It is to work with the Regulator to identify a flexible approach taking into account the particular circumstances of individual transactions and complementing the planned changes to the notifiable events framework and intends to document this in the updated Notifiable Events Code rather than in legislation.

*Our viewpoint*

*Again, we seem to be little further forward than in June when the proposals were first put out for consultation. The uncertainty for scheme sponsors and transaction planners continues.*

**Voluntary clearance**

The DWP has confirmed that the Pensions Regulator’s review of its clearance guidance will go ahead as proposed and that there are no plans to replace clearance with the declaration of intent.

**Improved Regulator Powers**

This is the “crime and punishment” section of the consultation response that has attracted most of the publicity. The now more or less settled civil and criminal sanctions are as follows:

New offence	New penalty	Target
Wilful or reckless behaviour in relation to a pension scheme	Criminal offence: up to 7 years’ imprisonment and/or unlimited fines  And/or new civil penalty of up to £1m	Sponsoring employers and others associated or connected

New offence	New penalty	Target
Failure to comply with a Contribution Notice	Criminal offence: unlimited fines  And/or new civil penalty up to £1m	Sponsoring employers and others associated or connected
Failure to comply with a Financial Support Direction	New civil penalty up to £1m	Sponsoring employers and others associated or connected (but not individuals other than controlling shareholders)
Failure to comply with the Notifiable Events Framework	New civil penalty up to £1m	Sponsoring employers and trustees
Failure to comply with requirements for a Declaration of Intent	New civil penalty up to £1m	Sponsoring employers and others associated or connected
Knowingly or recklessly providing false information to trustees	New civil penalty up to £1m	Any person who is required to provide information to trustees
Non-compliance with information requests (including inspections and interviews) or delays in providing information	Fixed and escalating civil fine	Any person targeted by the Pensions Regulator
Knowingly or recklessly providing false information to the Pensions Regulator	New civil penalty up to £1m	Any person who is required to provide information to the Pensions Regulator
Non-compliance with funding standards	Use of existing and strengthened powers	Trustees and sponsoring employers
Failure to provide a DB Chair's statement on time or of poor quality	Existing civil penalty	Trustees and sponsoring employers

This latest table is very similar to what had been proposed except that the maximum custodial term on conviction for wilful and reckless behaviour is set at 7 years, failure to comply with the Notifiable Events Framework will not be a criminal offence, and it is now clear which civil offences attract the up to £1m penalty (including newly, failure to comply with a Financial Support Direction).

### *Our viewpoint*

*Whilst thinking has moved on slightly in this area, we are still no nearer gaining an understanding of what it takes to be wilful or reckless in relation to a pension scheme, so it remains far from clear whether this headline grabbing offence will be any more than this.*

## **Anti-avoidance powers**

The June 2018 proposals to strengthen, clarify and improve the Pensions Regulator's anti-avoidance powers covering contribution notices and financial support directions are to go ahead but with some significant modifications.

### **Contribution Notices**

All four Contribution Notice (CN) proposals are to go ahead, but none without potential further work. The intention now is to:

- Amend the "reasonableness" test to reflect that the actual or potential impact of the act, or failure to act, on the value of the scheme's assets or liabilities, would be relevant when determining the amount to be paid under the CN (the previous proposal was for a "strong focus" on this factor).
- Add two additional limbs to the "material detriment" test so that the test is met if either the amount the scheme would have recovered on a hypothetical insolvency of the employer is materially reduced as a result of the act, or the employer's "value" provides materially less "coverage" of the scheme's section 75 deficit following the act.
- Protect the value of the CN from the date of the act – but it is not yet clear whether this will be through a specific uprating mechanism set out in legislation.
- Change the date on which the cap on the level of a CN is calculated, so that it is closer to the date of the final determination – but the details remain to be agreed with the Pensions Regulator.

### **Financial Support Directions**

The DWP is to go ahead with the creation of a single-stage process, under which a specific and enforceable obligation on the target would be created (rather than this occurring at some later stage as in the current regime) – and to reflect this change, the name of the regime will become Financial Support Notice (FSN).

In addition, the following are to go ahead:

- The "insufficiently resourced" test is to be replaced with a "scheme-focussed" test (no details given), on which the DWP needs to carry out further work with the

Pensions Regulator before setting it out in regulations. The current definition of a service company is also to be amended.

- The form of financial support the target is required to make to the scheme will be cash and/or joint and several liability (for the sponsoring employer's liabilities) in relation to the DB scheme – but there will still be scope for the target to agree an alternative form of financial support with the Pensions Regulator outside the formal FSN process.
- The Regulator will be provided with a power to impose a CN on any person associated or connected with the recipient of the FSN.

The following are not being taken forward:

- Providing the Regulator with a power to issue a FSD after a scheme has entered the PPF.
- Amending the reasonableness test to make clear that the actions of a target in creating or increasing risk are a relevant factor.
- Allowing FSDs to be issued to directors, but the DWP will extend the scope to capture controlling shareholders of the sponsoring employer who are individuals.
- Extending the “lookback” period (within which the “insufficiently resourced” test needs to be passed) from the current two years – but the DWP reserves the right to re-open this in the light of other changes.

### *Our viewpoint*

*This was the least developed part of the consultation and so we are not surprised to see some significant changes being announced, with the possibility of yet more as work progresses. What is worrying is that unlike other aspects of this consultation, there is no hint that there will be further consultation with the pensions industry. If this is intentional it is a grave mistake.*

## **Information gathering powers**

In the March 2018 White Paper the Government confirmed that it would harmonise and broaden some of the Pensions Regulator's information gathering powers to enable investigations to be carried out in a more efficient way. Although these powers were not part of the June 2018 consultation, the response provides some useful further information on them.

So, for example, when applying the new interview power the Pensions Regulator will have to give prior written notice explaining broadly the purpose of the interview and setting out the recipient's legal rights and responsibilities. And subject to certain exceptions any information gathered in this way may not be relied upon by the Pensions

Regulator as evidence for criminal proceedings or for issuing civil penalties. The Pensions Regulator intends to update and revise its existing compliance and enforcement policies document to include a statement of the legal context of when this interview power would be used.

The new system of fixed and escalating civil penalties will be implemented as proposed, with the DWP promising to engage with stakeholders regarding the appropriate level of these penalties and to consult on the regulations in due course.

### *Our viewpoint*

*So, to sum up, this consultation response reveals a work in progress, with some important detail yet to be fleshed out, or exposed for scrutiny. It is also completely silent on timescales for the delivery of any of the now revised proposals.*

*Despite nearly a year having passed since the White Paper it seems that the Pensions Regulator will have to rely on its existing powers until maybe April 2021 whilst these proposals are turned into a workable package. And for scheme sponsors, who are the main targets of this new regime, uncertainty continues.*

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