

New criminal offences and unlimited fines: what employers need to know about the Pensions Regulator's new powers

Updated February 2021

Pension briefing

HIGHLIGHTS

After the Carillion and BHS debacles, the Pensions Regulator (tPR) announced it was going to be "clearer, quicker and tougher". The new Pension Schemes Act 2021 (the Act), which received Royal Assent on 11 February 2021, gives tPR significant new powers so it can beef up its approach. Most provisions are not yet in force and we expect consultation on draft regulations and guidance before tPR's new powers have effect.

Corporate groups with defined benefit pension (DB) schemes should understand the Act's new requirements because failure to comply could result in large fines or being charged with a criminal offence.

For corporate groups with DB schemes, this is the most significant change in regulation since the Pensions Act 2004. The key message is be alert to anything that could weaken the financial position of the employers supporting the DB scheme or that could prejudice the DB scheme in an insolvency. In these circumstances, exercise caution and take advice.



NEW CRIMINAL OFFENCES AND FINES

The Act introduces two new offences punishable by up to seven years' imprisonment and / or an unlimited fine. The offences are:

- avoidance of a debt due under section 75 Pensions Act 1995 (known as a section 75 debt) – a person may commit this offence by doing an act (or failure to act) which, for example, prevents a section 75 debt becoming due or reduces the amount of a section 75 debt which would otherwise become due;
- committing an act (or failure to act) which "*detrimentally affects in a material way the likelihood of accrued scheme benefits being received*". The person must also have known, or ought to have known, that the act or course of conduct would have that effect; and not have a reasonable excuse.

The circumstances in which these new offences might be committed are wide-ranging and could catch normal corporate activity such as: an employer borrowing to fund working capital (whether on a secured or unsecured basis); payment of dividends and mergers and acquisitions.

A number of industry bodies (many of whom Hogan Lovells is actively involved with) have expressed concern about the potential breadth of these new offences.

CONTRIBUTION NOTICES (CN) – TPR'S POWER EXTENDED

A CN requires a one-off contribution to be made to the DB scheme and can be issued where there has been an act or deliberate failure to act which has:

- as a main purpose the avoidance of a section 75 debt; or
- the effect of detrimentally affecting in a material way the likelihood that scheme benefits will be received.

tPR must also be of the opinion that it is reasonable to issue a CN. tPR can take into account acts that took place up to six years earlier when deciding whether to issue such a notice.

Who can be subject to a CN?

tPR has the power to issue a CN to both the employer of a DB scheme and any person associated or connected with the employer. The latter will include, for example, group companies of the employer, shareholders who control more than one-third of the voting power in an employer and, in some cases, the employer's directors.

What's changing?

tPR's powers to issue CNs are being extended. There will be two new tests which, if satisfied, will also allow tPR to issue a CN. These are:

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

The *employer insolvency test* will be met (note this does not require an actual insolvency) if tPR considers that immediately after the person's act or failure to act (the "relevant time"):

- the value of the scheme assets was less than the amount of the liabilities (as estimated by tPR, on the buy-out basis); and
- if a section 75 debt had fallen due from the employer, the person's act (or failure to act) would have materially reduced the amount of the debt likely to be recovered by the scheme.

The employer resources test will be met if tPR considers that:

- the act (or failure to act) reduced the value of the employer's resources; and
- that reduction was a "material reduction" relative to the amount of the estimated section 75 debt which would be due from the employer had the scheme started winding up.

Again, these tests could capture normal corporate activity. There will be a statutory defence to the above tests, which requires, very broadly, the person to have: considered the issue; taken steps to minimise the impact (where relevant); and reasonably concluded that there would not be such a reduction.

The Pensions Act 2004 (the 2004 Act), which introduced CNs, allowed tPR to issue a CN in respect of an act that took place before the 2004 Act became law. The Pensions Minister has recently told Parliament that provisions in the new Act will not be retrospective – but this is not explicit on the face of the new provisions. Further detail on how the new powers may be exercised can be expected in draft regulations and guidance.

EXTENSION OF THE NOTIFIABLE EVENTS REGIME

Legislation already requires employers to notify tPR of certain events affecting the employer, for example, a decision by a controlling company to relinquish control of the employer. However, in our experience, notification can sometimes be an afterthought or even forgotten entirely.

The list of notifiable events will be extended. Details of the additional notifiable events will be set out in regulations (which have not yet been issued), but we expect the list to include sale of a material part of a sponsoring employer and giving security to creditors ahead of the DB scheme. Notification will need to include an analysis of the impact on the pension scheme and steps taken to mitigate any adverse effects.

The obligation to notify applies to both the employer and any person connected or associated with the employer. Failure to comply could give rise to a fine of up to £1 million.

HOW WE CAN HELP

Through our active participation in the pension industry and involvement in some of the highest profile cases involving DB schemes, we can give you an informed view on tPR's approach and how that develops in light of these new powers. We can also help you build corporate processes and design solutions that do not fall foul of the new regime.

This note is written as a general guide only. It should not be relied upon as a substitute for specific legal advice.

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