

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

Updated August 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 further 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.

We have updated this note to cover recent consultations on draft regulations and on tPR’s draft policy explaining how it will investigate and prosecute the new criminal offences.



## 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.

The offences will only be committed if the person did not have a reasonable excuse (which will be for the prosecution to prove).

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.

## Draft investigation and prosecution policy

tPR has recently consulted on a draft policy setting out its approach to investigating and prosecuting the new offences. tPR makes clear that it expects those it investigates to explain their actions and to put forward evidence of any matters which might constitute a reasonable excuse. In particular, it expects the reasons behind particular action (or inaction) to be well documented, including consideration of alternative approaches and any assessment that no material detriment would arise. Having a clear audit trail will be important.

When assessing whether a person has a reasonable excuse, tPR will consider three factors in particular:

- Whether the detrimental effect was an “*incidental consequence*” of the act (or omission), or a “*fundamentally necessary step to achieve the person’s purpose*”. The more the detriment is incidental, the more likely the person would be to have a reasonable excuse.
- The adequacy of any mitigation to offset the detrimental effect.
- Where there was no (or inadequate) mitigation, was there a “*viable alternative*” which would have avoided or reduced the detrimental effect? For example, there may be no viable alternative where new secured debt is critical to the employer’s survival and the continuation of the employer is a better outcome for the scheme than the employer’s insolvency.

## 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.

Following consultation, the DWP has confirmed that an employer's resources for the purposes of this test will be its profits before tax, adjusted to exclude the effect of non-recurring or exceptional items. It will be for tPR to decide whether an item is non-recurring or exceptional, its value and

the effect of the act (or failure) on the employer's resources. The pension industry has raised concerns about the lack of clarity about how the test will be applied.

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.

### WHEN WILL THE CHANGES COME INTO FORCE?

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. It would be helpful for the commencement orders (which will bring the provisions of the Act into force) specifically to prevent retrospective application.

In tPR's draft prosecution policy, it states that evidence predating the commencement date of the legislation (expected to be 1 October 2021) may be relevant to its investigation or prosecution of actions after that date, for example if it indicates a party's intention.

### 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.

## KEY HOGAN LOVELLS PARTNERS

<b>Katie Banks</b>	<b>+44 20 7296 2545</b>	<b>katie.banks@hoganlovells.com</b>
<b>Duncan Buchanan</b>	<b>+44 20 7296 2323</b>	<b>duncan.buchanan@hoganlovells.com</b>
<b>Claire Southern</b>	<b>+44 20 7296 5316</b>	<b>claire.southern@hoganlovells.com</b>
<b>Edward Brown</b>	<b>+44 20 7296 5995</b>	<b>edward.brown@hoganlovells.com</b>
<b>Faye Jarvis</b>	<b>+44 20 7296 5211</b>	<b>faye.jarvis@hoganlovells.com</b>



### **Pensions360:** the full picture

[www.hoganlovells.com/pensions360](http://www.hoganlovells.com/pensions360)

#### **About Pensions360**

Hogan Lovells' broad cross-practice capability covers the full spectrum of legal advice from lawyers who understand pension clients; advising on issues from scheme investments, corporate restructurings and transactions, to funding solutions and interaction with the Regulator or the courts. The ability to draw on specialists from other practices who are not only experts in their field but have an in-depth understanding of pension issues sets us apart from our competitors.

## [www.hoganlovells.com](http://www.hoganlovells.com)

"Hogan Lovells" or the "firm" is an international legal practice that includes Hogan Lovells International LLP, Hogan Lovells US LLP and their affiliated businesses.

The word "partner" is used to describe a partner or member of Hogan Lovells International LLP, Hogan Lovells US LLP or any of their affiliated entities or any employee or consultant with equivalent standing. Certain individuals, who are designated as partners, but who are not members of Hogan Lovells International LLP, do not hold qualifications equivalent to members.

For more information about Hogan Lovells, the partners and their qualifications, see [www.hoganlovells.com](http://www.hoganlovells.com).

Where case studies are included, results achieved do not guarantee similar outcomes for other clients. Attorney Advertising.

© Hogan Lovells 2021. All rights reserved. [LIB02/BANKSKAT/9724887.8]