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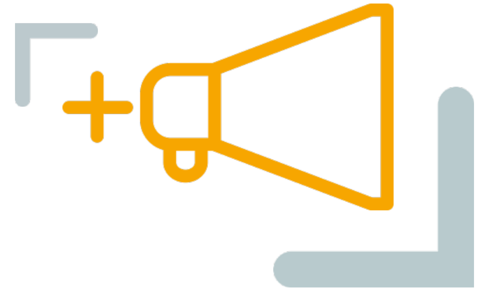

News Alert 2020/01

8 January 2020

The Pension Schemes Bill is back

At a glance

On 7 January progress started once more on the Pension Schemes Bill when it returned to the House of Lords to receive its First Reading – a formality ahead of its republication on 8 January. The Bill is substantially the same to that introduced in October and which fell away following the calling of the General Election, but there is the prospect of more being added during the Bill's parliamentary journey. In this News Alert, we summarise and comment on the contents of the Bill which will presumably get on to the statute book by the early summer.

The Detail

Collective money purchase schemes

A large part of the Bill is devoted to introducing legislation to allow what were called Collective Defined Contribution Schemes to come into existence. Now referred to as Collective Money Purchase schemes (CMPs), this largely unchanged part of the Bill introduces an authorisation and supervision framework intended to allow the proposed Royal Mail scheme to come into existence with most of the detail to be set out in regulations.

An authorisation and supervision framework is introduced for a new form of risk sharing scheme

Further detail about the Bill's provisions in respect of these schemes is set out in the Appendix.

Contribution notices, criminal offences and new civil penalties

Turning to DB schemes, there are some significant additions to and adjustments of the current powers that the Pensions Regulator has in relation to issuing notices to corporate targets demanding that they make substantial payments to schemes, but surprisingly nothing on financial support directions that were to be completely overhauled. The spectre of jail time for interfering with the financing of schemes is also raised.

Significant additions and adjustments are made to the contribution notice legislation

Two new contribution notice triggers

Contribution notices will now be possible if either an "employer insolvency test" or an "employer resources test" is failed. The first new test is where an act or failure to act *"would have materially reduced the amount of the (section 75) debt likely to be recovered*

by the scheme". The second new test is where an act or failure to act *"reduced the value of the resources of the employer"* and *"that reduction was a material reduction relative to the amount of the estimated section 75 debt in relation to the scheme"*.

There is a statutory defence – "the ABC defence" – available to targets of the new contribution notices. If they can demonstrate that they gave due consideration in advance to the impact of the act or failure to act and either concluded that there was no material reduction in the recoverable debt/employer resources or else provided appropriate mitigation against any reduction then that will be a legal defence. The existing clearance mechanism will also continue to be available.

Sum specified in the contribution notice and its due date

The "relevant time" as at which the Regulator estimates the section 75 debt, which informs the amount that would be due under a contribution notice, is defined. Currently it is thought to be when the trigger event occurred. Relevant time will now be simply the end of the scheme year which ended most recently before the day on which the Regulator gives a determination notice in respect of an intended contribution notice. This could have a dramatic impact on the amount set out in a contribution notice and applies to both the existing and new contribution notices triggers.

Separately, failing to pay any contribution notice by its due date will constitute either a criminal offence leading to a fine or attract a new scale of civil financial penalties of up to £1m.

Two new criminal offences

Including related new criminal offences

A new criminal offence of the "avoidance of employer debt" occurs if a person prevents the recovery of all or part of a section 75 debt, prevents it from becoming due, compromises or otherwise settles the debt or reduces the debt (and intended to do so).

Conduct risking accrued benefits is also a new criminal offence defined as an *"… act or course of conduct that detrimentally affects in a material way the likelihood of accrued scheme benefits being received"* without reasonable excuse and where the person committing the act knew or ought to have known that that the act or course of conduct would have that effect.

These two offences mirror the existing triggers for a contribution notice. Both new offences can result in an unlimited fine and/or up to seven years in jail. Alternatively, the Regulator can deal with similar transgressions by means of financial penalties of up to £1m.

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Our viewpoint

The two new contribution notice triggers are designed to be easier for the Regulator to use than the current two triggers. There is significant uncertainty at this stage as to what scenarios are potentially in scope but initial impressions are that a wide range of business as usual corporate activity could be affected. Moreover, the new contribution notice powers may operate retrospectively. Employers now considering activity such as business sales or debt re-financing that may affect the pension scheme should take advice on the risk that they may be impacted by this legislation.

It appears that the new criminal offences replace the "wilful or reckless behaviour in relation to a pension scheme" offence that seemed to have been settled on in 2019. Worryingly they seem to be much wider in scope, including who is potentially caught.

Notifying the Regulator of significant corporate events

The notifiable events legislation is expanded

The notifiable events legislation impacting PPF-eligible schemes is expanded, requiring employers to give notice to the Regulator of certain events, material changes to the effect of such events and the non-occurrence of these events. These notices must be given "as soon as reasonably practicable" and a regulation-making power is introduced to enable notification to be required from a prescribed earlier date. As for the events themselves, although the detail will be in the regulations, according to an impact assessment the events will be as settled following the June 2018 consultation.

Including new statements of intent in relation to three types of corporate events

The Bill also includes the provisions for "statements of intent" that employers must supply to the Regulator at the same time as notifying three particular events. The impact assessment suggests that these events are as settled following the June 2018 consultation – ie 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. The statements of intent, which must also be sent to the trustees, describe the event, any adverse effect of the event on the scheme, any steps taken in mitigation and any communication with the trustees.

Our viewpoint

That the Government is going ahead with the adjustments to the notifiable events legislation and introducing statements of intent in respect of certain corporate events is no surprise. But it will be some time before we find out how onerous these new requirements will be and to gauge their impact on corporate activity

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Other Regulator powers

The Regulator's powers are expanded in the area of interviews and inspection of premises. A fixed and escalating penalty regime is introduced where information requests and the like are not complied with.

The Regulator's powers are expanded in other areas, including new financial penalties

Financial penalties are potentially imposed where a person has *"knowingly or recklessly provided the Regulator with information which is false or misleading in a material particular"* in connection with specified obligations. The same sanction potentially applies where a person has acted similarly towards the trustees of a DB scheme in relation to specified obligations they have to the trustees.

New provision is made for financial penalties to be meted out by the Pensions Regulator of up to £1m, with the possibility of regulations delivering higher limits. Aimed at corporates, the fine can be personal.

Our viewpoint

None of these new powers are a surprise – in some cases what is surprising is that the Regulator did not already have such powers. We are hoping that the Regulator will use these new powers in a proportionate manner.

Pension dashboards

A number of clauses set out what constitutes a "qualifying pensions dashboard service" before going on to enable regulations to be set that will require occupational pension schemes (of any type) to supply data to the dashboard providers, with the threat of sanction from the Pensions Regulator for failing to do so. The FCA is also empowered to set rules to require personal and stakeholder pension providers to supply data. Schemes may need to provide generic scheme information and *"information as regards the position of an individual in relation to the scheme"*.

Pension dashboards are given necessary framing legislation

Our viewpoint

It is likely to still be some time before schemes will need to supply data to the pensions dashboard, but this first mention in legislation is a sign that the dashboard project will be delivered over the course of the next few years. Quite how onerous this is going to be for schemes in their role of contributing data remains unanswered.

DB scheme funding

Trustees will need to agree with the employer a long-term "funding and investment strategy" which must in particular specify the funding level that the trustees intend the scheme to have achieved by a "relevant date(s)" and the investments they intend the scheme to hold at that time. This strategy will be constrained by regulations almost certainly linked to the new DB funding code.

Significant changes are made to the DB scheme funding legislation, with more to come

Having settled this strategy, the trustees will need to prepare a written statement of this strategy which also must contain certain supplementary matters such as the extent to which the trustees think the strategy is being successfully implemented (and, where not, proposed steps to remedy this), the main risks faced by the scheme in implementing the strategy and how the trustees intend to mitigate or manage them and the trustees' reflections on any relevant significant decisions taken by them in the past. This "statement of strategy" must be signed by the chair of trustees. Employers need to be consulted but do not need to agree the statement.

Other changes include the following:

- The scheme's technical provisions must be determined in a way that is consistent with the scheme's funding and investment strategy as set out in the statement of strategy.
- The trustees must send all scheme funding valuation reports to the Regulator after they have received them.
- Regulations are likely to set out the matters to be taken into account or the principles to be followed in determining whether a recovery plan is "appropriate".

Our viewpoint

The proposed changes to the primary legislation cover only part of what is likely to be a sweeping reform of the regulation of DB scheme funding with potentially significant impacts on the current flexibility for negotiating journey plans and technical provisions and determining investment strategies. But the impact of the whole package will be very much scheme-specific.

We wait to hear from the Regulator as to when it will launch its much-anticipated first consultation on the DB Funding Framework.

Other provisions

Transfer values

The legislation governing the right to take a "cash equivalent" is constrained with the objective of enabling trustees who have doubts whether the destination scheme is genuinely occupational by reason of the individual's new "employment", to deny a transfer to that scheme. Details will be spelt out in regulations.

Schemes will have greater powers to deny transfers where they have doubts about the destination scheme

Our viewpoint

It is now more than three years since the Government first proposed this measure. We wonder how many fraud victims' pensions could have been saved if the Government had acted with more urgency.

The Pension Protection Fund

A very short clause expands the effect of changes made by regulations to overcome the Beaton case in relation to fixed pensions granted on transfer in (see Pensions Bulletin 2018/36). The regulations, which are currently effective only for schemes entering assessment since 2 October 2018, will be deemed to always have had effect.

Our viewpoint

The Bill represents the culmination of a substantial amount of policy work bringing forward most of the measures discussed in the March 2017 Green Paper and the February 2018 White Paper. But there are some significant omissions – most notably in relation to the promise to set up an authorisation and supervision regime for the new DB consolidation vehicles.

Other areas that have failed to make the cut include adjustments to the GMP conversion legislation in order to facilitate its use as an equalisation solution and changes to the Pensions Ombudsman's powers and duties in order to reflect his expanded role and new ways of working. It will be interesting to see if any of these find their way into the Bill as it starts its passage through Parliament in earnest.

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Lane Clark & Peacock LLP
London, UK
Tel: +44 (0)20 7439 2266
enquiries@lcp.uk.com

Lane Clark & Peacock LLP
Winchester, UK
Tel: +44 (0)1962 870060
enquiries@lcp.uk.com

Lane Clark & Peacock Ireland Limited
Dublin, Ireland
Tel: +353 (0)1 614 43 93
enquiries@lcpireland.com

Lane Clark & Peacock Netherlands B.V. (operating under licence)
Utrecht, Netherlands
Tel: +31 (0)30 256 76 30
info@lcpnl.com

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Appendix

Collective money purchase schemes – the detail

How CMPs will work

In their simplest forms, CMPs work by providing "qualifying benefits" whose value is periodically balanced with the value of the pension scheme assets. In the Royal Mail scheme, this is achieved in all but extreme cases by adjusting the level of future pension increases both before and after retirement – so if experience is good all future increases go up and if it is bad they go down. If funding gets really bad, benefits can be cut and potentially the scheme can be forced to wind up.

If the scheme wants to provide any guaranteed benefits, such as guaranteed lump sums on death, they have to be provided by a completely separate section of the scheme with no cross-funding.

Only single employer schemes, or those run by "connected" employers within the same group, are allowed. Public service employers are excluded, but there is the facility for regulations to extend the definition of "qualifying schemes" to multi-employer schemes and Master Trusts.

Transfers out of the scheme are to be allowed. Regulations will set out further rules on elements such as the calculation of benefits, member communications, and the significant events that should be notified to the Regulator.

Authorisation, benefit calculation and regulation

All CMPs need to be authorised by the Pensions Regulator, with applications meeting the following authorisation criteria:

- Certain key figures in the scheme, including the person establishing the scheme and the trustees, meet "fit and proper persons" requirements.
- The trustees confirm in a "viability report" the design of the scheme and why they consider it to be sound. This report will be reviewed annually. A scheme actuary is required to advise on the method and assumptions used, provide a "viability certificate" confirming the design of the scheme is sound and carry out the annual valuations assessing the balance between assets and liabilities.
- The scheme has an adequate "continuity strategy", which outlines how it could react to one of a number of "triggering events", including employer insolvency, scheme closure or wind up and the Regulator shutting down the scheme.
- The scheme should be financially sustainable, including by having sufficient resources to cover the costs of set up and running the scheme.

- The communications are adequate so that correct and not misleading information is sent to members, prospective members and survivors.
- The scheme has effective systems and processes to ensure the scheme runs smoothly.

The Pensions Regulator will keep a list of all authorised CMP schemes and has quite wide-ranging powers to take steps it sees appropriate if something goes wrong. It can call a new valuation or issue a "risk notice" if it is concerned the scheme might breach the authorisation criteria and require the trustees to submit proposals for fixing the issues by a specified date. In extreme cases, withdrawal of authorisation is possible.

Triggering events

If a triggering event does occur, a scheme has one of the following three continuity options:

- Discharge of liabilities and winding up – either by transferring to another CMP, a DC Master Trust or other specified scheme.
- Resolving the triggering event (eg, on employer rescue if it became insolvent).
- Conversion to closed scheme, with Regulator approval. This decision cannot be reversed.

In certain scenarios, the trustees must pursue the first option. Under any of the above options, the trustees must generally submit an "implementation strategy" to the Regulator setting out how members' interests will be protected, which the Regulator should approve, followed up by regular reporting after the event.

Our viewpoint

The Bill provides a sensible-looking framework for Collective Money Purchase schemes to sit within. Whilst employers interested in the concept don't have enough information to set up a scheme at this stage, they do have a good steer as to where the Government is going. Indeed, such employers might benefit from investigating the concept now and being able to ensure any specific features they would appreciate