UK: PENSIONS UPDATE – JANUARY 2020

1. PENSION SCHEMES BILL 2019-2020

1.1 **The Pension Schemes Bill[1] (the Bill) which was originally introduced in October 2019, was reintroduced by the Queen's Speech on 19 December 2019 with only minor amendments and no real change to the substance of the Bill.**

1.2 The Bill covers a wide range of modifications, including a framework for collective defined contribution schemes and pensions dashboards; a new requirement for trustees to determine and prepare a written statement of the scheme's long term funding and investment strategy; a criminal fine for failure to comply with a CN and new circumstances in which CNs can be issued; and increased information gathering powers for the Pensions Regulator (which includes a new requirement for persons associated and connected with scheme employers to give notice of certain events). The Bill reflects the Government's intention to create a stronger Pensions Regulator (tPR) as consulted on in July 2018, and many of the changes (albeit not all) reflect those set out in the Government's proposals - see our July 2018 Special Edition briefing for details.

1.3 As we reported in our October 2019 Special Edition briefing, of key interest is likely to be the proposed criminal offence for engaging in conduct that "*detrimentally affects in a material way the likelihood of accrued benefits being received*", which carries with it a maximum custodial sentence of up to 7 years and which goes beyond the criminal sanction that had previously been trailed by the Government. Please see our October 2019 Special Edition briefing for further details.

1.4 This briefing below considers some of the other aspects of the Bill that are also likely to be of interest.

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Criminal Offence – avoidance of employer debt	
Akin to the criminal offence of risking accrued scheme benefits and also attracting a custodial sentence of up to 7 years, is the offence committed by a person where (on a criminal burden of proof) they:	
(a)	do an act or engage in a course of conduct (including a failure to act) that (i) prevents the recovery of the whole or any part of a Section 75 Debt, (ii) prevents such debt becoming due, (iii) compromises or otherwise settles such debt, or (iv) reduces the amount of such debt which would otherwise become due;
(b)	they *intended* the act or course of conduct to have such effect; and
(c)	they did not have a "*reasonable excuse*" for the act or for engaging in the conduct.

[1] https://publications.parliament.uk/pa/bills/lbill/58-01/004/5801004.pdf

Of particular note is that the scope of the offence is not limited to employers and/or associates of employers (it applies simply to "persons" who, theoretically at least, could be anyone involved with an occupational defined benefit pension scheme, including trustees, advisers and investment counterparties). The offence (presumably intentionally) does not require any detriment to have occurred in respect of the scheme so in practice many legitimate steps taken by those associated with pension schemes (e.g. making deficit repair contributions, entering into Flexible Apportionment Arrangements) would meet the conditions in both (a) and (b) above and bring persons involved with such steps within the remit of the offence.

However, we expect that many persons involved with occupational defined benefit pension schemes will be able to build a "reasonable excuse" defence for their conduct and it will be for the Courts to determine whether this criteria has been met on the basis of an objective test.

Criminal Offence – failure to pay a CN

The Bill also criminalises a persons failure to pay a CN, absent a "*reasonable excuse*" for not doing so. Again, whether this defence is made out will be an objective test for the consideration of the Courts.

1.5 Prosecution of the new criminal offences in the Bill may be instituted by tPR, the Secretary of State or the Director of Public Prosecutions without the preliminary warnings or regulatory appeal process that apply in the existing CN regime. There is no suggestion that the offences will be linked to a Pensions Regulator Code of Practice to more clearly define the parameters within which the offences would be prosecuted (though at the very least we would expect the pensions Regulator to apply or update its existing prosecution policy in relation to other pensions related criminal offences (e.g. in the context of auto-enrolment), pursuant to which it has regard to the Code for Crown Prosecutors and which in turn requires certain evidential and public interest tests to be satisfied).

Other Changes to CNs

The Bill introduces two new grounds for imposing a CN:

- the "*employer insolvency test*": broadly, this may apply where tPR is of the opinion that, at the time of an act, (i) the pension scheme was in deficit; and (ii) if a section 75 debt had fallen due immediately after the act, this act or failure to act "*would have materially reduced the amount of the debt likely to be recovered by the scheme*", and
- the "*employer resources test*": broadly, this may apply where tPR is of the opinion that an act or failure to act reduced the value of the resources of the employer and that reduction was material relative to the amount of the estimated section 75 debt in relation to the scheme. (Note this latter test reflects the Government's proposals as expressed in its 2018 consultation.)

This potentially significantly extends the range of circumstances which can give rise to a CN being issued – albeit, as now, tPR would need to be of the view it is "reasonable" to impose a CN.

As trailed by the Government the "reasonableness" test has also been amended to enable TPR to give a stronger focus on the loss caused to a scheme by the act or failure to act.

Expansion of the Notifiable Events Regime

The foreshadowed 'declaration of intent' regime is captured in the Bill through changes to the existing notifiable events requirements. The Bill requires (unless tPR otherwise directs) "the appropriate person" (being the employer, its associates and connected persons and other prescribed persons) to give a notice, along with an accompanying statement, of the notifiable event to tPR and a copy of the notice and statement to the trustees or managers at the same time. Much of the detail has been left to regulations, but as a minimum the statement must explain the nature of the event, what the adverse effects on the pension scheme (if any) are and the steps taken in mitigation and describe any communication with the trustees or managers about the event.

The Bill also provides that regulations may require notice to be given (to tPR and the trustees) a prescribed period of time in advance of the relevant event or material changes to the event. Employers and their associates/connected parties (e.g. large shareholders, group companies and individual directors) may therefore be subject to a much more onerous and prescriptive information sharing regime in relation to certain corporate activity – and direction will be required from tPR to avoid significant duplication.

Higher Civil Penalties For More Serious Offences

The Bill also empowers tPR to impose financial penalties of up to £1million for more serious offences (not to apply where a person has already been convicted of a criminal offence for the same act – noting here that the new criminal offences (including those attracting custodial sentences) may result in unlimited fines). The offences include:

- failure to comply with a CN;
- avoidance of an employer debt and conduct risking accrued scheme benefits;
- failure to comply with the notifiable events framework; and
- the deliberate provision of false information to tPR/trustees.

Other Criminal Offences

Amendments to Section 80 of the Pensions Act 2004:

- Section 80 of the Pensions Act 2004 currently provides that a person who knowingly or recklessly provides tPR with false or misleading information in purported compliance with any of the requirements listed in that section may be guilty of a criminal offence punishable by a fine, or up to 2 years imprisonment, or both.
- The Bill extends the remit of section 80 to include where the information has been provided to tPR in purported compliance with the notifiable events regime (as expanded by the Bill).

Amendments to Section 77 of the Pensions Act 2004:

- The Bill also criminalises the offence where a person, without reasonable excuse, neglects or refuses to (i) attend an interview with tPR as required; or (ii) answer questions at such interview with tPR.
- The offence is punishable by a fine.

New Funding and Investment Strategy Requirement

Trustees will be required to determine, review and (if necessary) revise, a "*funding and investment strategy*" for ensuring benefits can be provided over "*the long term*". This strategy must be set out in a written "*statement of strategy*", which must also cover supplementary matters (e.g. the opinion of the trustees as to the success of implementation of the strategy and the risks associated with it and how they will mitigate them). The strategy must specify the funding level the trustees or managers intend the scheme to have achieved as at the relevant date(s) and the investments the trustees or managers intend the scheme to hold on such date(s).

Some key points to note:

- Much of the detail around this requirement (e.g. the level of detail required in the strategy, time periods and the factors to be taken into account when reviewing a strategy) is to be included in regulations.
- A scheme's technical provisions will be required to be calculated in a way that is consistent with the statement of strategy. (However, it remains to be seen how this will interact with the existing principles for

calculating technical provisions under the Scheme funding legislation, which will continue to require a justification for any changes to a scheme's methods and assumptions as compared to those used on the last occasion on which they were calculated).

- Employer agreement is required to the funding and investment strategy, as set out in the statement of strategy. While the SIP will remain the purview of trustees, this may give employers some greater influence than they have currently.
- The Pensions Regulator may exercise its powers under section 231 of the Pensions Act 2004 to give a direction requiring trustees to revise their scheme's funding and investment strategy (it is not clear whether this power would still be exercisable where the trustees and employer have agreed the funding and investment strategy).

2. STATUS UPDATE ON PENSIONS REGULATOR'S DB FUNDING CODE

2.1 We understand that tPR intends for its revised funding regime to be in force by the end of 2020/ early 2021. To achieve this, tPR plans to issue the first consultation on its new regulatory approach (see below) in early 2020, followed by draft regulations from the Department of Work and Pensions (DWP). TPR expects to issue its second consultation on the revised draft Defined Benefit Funding Code in the spring/summer of 2020.

TPR's Defined Benefit Funding Code now expected in Spring/ Summer 2020

2.2 We understand tPR's proposal is to create a dual-route approach for the regulation of the funding arrangements for defined benefit pension schemes. The "fast-track" route will be available for those schemes whose funding package is tPR compliant and so does not require tPR engagement, and the "bespoke" route will be available for those schemes taking an approach outside of the prescribed guidelines which will necessitate tPR scrutiny to check that they have the evidence base to support diverging from fast-track.

2.3 It remains to be seen how tPR will balance its scrutiny of the bespoke route schemes (which are likely to be significant in volume) without appearing to take on an advisory role in relation to such schemes.

3. EXPANSION OF REGISTRATION REQUIREMENTS FOR EXPRESS TRUSTS

3.1 The Fifth Money Laundering Directive (5MLD)[2] which amends the Fourth Money Laundering Directive (4MLD), came into force at an EU level on 9 July 2018 – the UK had until 10 January 2020 to transpose the requirements into UK law. 4MLD placed a requirement on the UK to create a register for all express trusts that incur a UK tax consequence. As a result, HMRC set up the Trust Registration Service (TRS). For persons operating express trusts in the UK (or looking to establish new express trusts), it is important to be aware that, among other things, 5MLD expands the scope of HMRC's TRS, by requiring trustees or agents of all UK (and some non-EU resident express) trusts to register these trusts with the TRS, whether or not the trust has incurred a UK tax consequence (NB Member States have until 10 March 2020 to set up the revised beneficial ownership registers for trusts).

All existing UK express trusts are suggested to be registered by 31 March 2021 and new trusts created after 1 April 2020 are suggested to be registered within 30 days

3.2 In April 2019, the Government consulted on how to implement the requirements of 5 MLD, with the promise of a more detailed technical consultation run by HMRC later in 2019. While money laundering regulations were brought into force in December 2019, they do not address the trust registration requirements and the Government is yet to publish its response to consultation now expected in early 2020) and HMRC's technical consultation is still awaited.

3.3 It is not expected that pension scheme trusts will be excluded from this requirement (as no exclusion is mentioned in the consultation or in 5MLD itself), but we would note that in 2017 HMRC took the pragmatic approach to 4MLD that registered pension schemes did not separately have to register with the TRS - it is hoped a similar pragmatic solution can be found in respect of 5MLD.

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2 (EU) 2018/843

3.4 In any event we would highlight that the Government states in its April 2019 consultation that the registration requirements will not apply to existing trusts until 31 March 2021 and for trusts created on or after 1 April 2020, a deadline of 30 days from creation to be registered is suggested.

4. PSF V BAUER[3] – IMPLICATIONS FOR PPF COMPENSATION LEVELS

4.1 The Court of Justice of the European Union (CJEU) handed down its judgment in the Bauer case on 19 December 2019. Broadly the CJEU held that, if the reduction in a member's benefits applied by the lifeboat body of a Member State (in the UK's case, the Pension Protection Fund (PPF)) would result in that individual having to live "*below the at-risk-of-poverty threshold determined by Eurostat for the Member State concerned*", the Member State is obliged to ensure a minimum degree of protection for the member (i.e. to provide benefits above the at-risk-of-poverty threshold, even where the individual receives at least 50% of their benefits).

4.2 Our understanding is that the UK's at-risk-of-poverty threshold as determined by Eurostat for 2018 is equivalent to about £11,142 per year - in practical terms it is not obvious how many (if any) of the PPF's members will fall below this threshold. However, for those that do, query how the PPF is going to approach determining whether a particular member should receive higher benefits? (For example, will the onus be on the member to evidence total income) and how will this be checked?

4.3 It is clear that the judgment does not require the PPF to provide 100% of benefits to members under EU law (contrary to the recommendation of the AG opinion in this case) but that as a minimum, every individual must receive at least 50% of their accrued benefits. In light of this, the PPF has confirmed that it considers its implementation methodology announced following the CJEU's judgment in the *Hampshire*[4] case (being to ensure members receive at least 50% of the value of their accrued benefits), meets this minimum requirement.[5] It remains to be seen how the PPF will implement the remainder of the judgment, and the PPF has stated that it will work through "*the other details of the judgment*" with the DWP in order to do so.

5. DWP CONSULTS ON GENERAL LEVY INCREASE

5.1 On 18 October 2019, the DWP published its annual review of the general levy (General Levy) on pension schemes. The consultation closed on 29 November 2019 and a response to consultation is awaited.

5.2 The General Levy is intended to recoup the DWP's funding of tPR, the Pensions Ombudsman and pensions-related activities of the Money and Pensions Service, who each receive a grant-in-aid from the DWP. The General Levy applies to both occupational and personal pension schemes, with charges varying according to the number of scheme members. Exact levy rates have remained the same for most schemes since they were last set in 2012/13. A new, lower, levy rate for schemes with 500,000 members or more was introduced in 2017 to 2018.

According to the DWP consultation, as a result of factors including a failure to keep up with inflation and significant changes in the pensions industry and regulatory landscape, a deficit of over £50 million is projected for 2020/21.

What is the DWP Proposing?

5.3 The DWP has proposed four options for the 2020/21 levy year to resolve the deficit and align funding/ expenditure going forwards:

1. *Increasing levy rates by 10% on 1 April 2020, with further increases from April 2021* informed by a wider review of the levy with an industry working group (this is the DWPs preferred option and would involve a further consultation on how to increase the General Levy from 2021 onwards);
2. *Introducing a phased increase over the three years from 1 April 2020* (this is not the DWPs preferred approach as it would require substantial increases in the General Levy in years 2021/22 to 2022/23);

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3 *Pensions-Sicherungs-Verein VVaG v Gunther Bauer [2019] (Case C-168/18)*

4 *Grenville Hampshire v The Board of the Pension Protection Fund* [2018] (Case C-17/17)

5 See our UK Pensions Update: October 2019 edition for more details

3. *Introducing a phased increase over approximately ten years from 1 April 2020* (the DWP does not say how it feels about this option. It would allow for more gradual realignment of the levy rates but note that the DWP would still consult annually on the General Levy and so the approach would be subject to change);

4. *Introducing a phased increase over approximately ten years from 1 April 2021* i.e. there would be no increase for the 2020/21 levy year (the DWP does not say how it feels about this option. While resulting in slightly higher annual increases than the option above, this offers a longer-term solution while recognising that some pension schemes may prefer a longer notice period in advance of the first increase).

5.4 In addition, the DWP proposes a one-off increase in the flat-rate levy paid by small schemes with between two and 11 members. For occupational schemes in this category, the annual levy would rise from £29 to £75 per scheme, while for personal schemes the annual levy would increase from £12 to £30 per scheme.

5.5 Industry responses to the proposals have been negative (in particular given the fact that the levy is calculated per pot and so it appears that mastertrusts and other automatic enrolment schemes with low earners with multiple pots are likely to be the worst hit) and the general consensus appears to be that a wider review of the levy structure is needed.

6. CJEU EQUALISATION DETERMINATION - SAFEWAY

6.1 The CJEU gave its decision in the Safeway[6] equalisation case on 7 October 2019. The CJEU confirmed that Safeway is not allowed to equalise normal retirement ages retrospectively to the date of a member announcement that was issued prior to the date of the deed of amendment which was executed to amend the scheme rules (despite the fact that the scheme rules expressly permitted amendments made in such a way).

6.2 The CJEU confirmed that such retrospectivity would be against EU principles of law, including that of legal certainty which requires that members' rights under a pension arrangement must be implemented in a way that is sufficiently precise, clear and foreseeable to enable the persons to know their rights and be able to rely on them.

6.3 A surprising aspect to the judgment is the idea that, according to settled case law, retrospective equalisation may be possible in exceptional circumstances where there is an objective justification, provided that the legitimate expectations of the persons affected are respected and there is otherwise a risk of "*seriously undermining the financial balance of the pension scheme*".

6.4 Because Safeway had not made the argument that retrospective equalisation was necessary to prevent the financial balance of the Safeway pension scheme from being seriously undermined, the CJEU concluded that there seemed to be no objective justification to allow retrospective equalisation. However, it seems to have left the door open for the Court of Appeal to conclude otherwise.

6.5 The case has now returned to the Court of Appeal with a hearing listed for 2 July 2020. It remains to be seen what guidance the Court of Appeal will be able to draw from the "settled case law" referred to by the CJEU (the cases referred to concerned the social security systems of the Member States concerned, not private pension arrangements, and the economic arguments failed in both cases) and what weight will be given to the funding position of the scheme as well as the financial circumstances of the employer.

7. PENSIONS OMBUDSMAN DETERMINATION IN EMPLOYER DUTY CASE[7]

7.1 The Deputy Pensions Ombudsman has rejected a complaint by a member (Mr T) of the Principal Civil Service Pension Scheme (PCSPS) that he was denied the opportunity to make an informed decision about whether to transfer his past service benefits from the transferring scheme (Capgemini) to the PCPS as a result of his employer's delay in providing him with clear, full and timely information about his transfer options.

7.2 In summary, the member had been the subject of several TUPE transfers throughout his career, the last of which took place in December 2015, a few months prior to his normal retirement date of 60. His pension benefits

6 Safeway Ltd v Newton C-171/18

7 (PO-25827)

remained in the transferring scheme, but in March 2016 he was given some information regarding a bulk transfer of such benefits to the PCSPS (although details were not available at that time as they were not finalised until April and in particular Mr T was not aware that transferees were to be awarded an additional service credit as part of the bulk transfer). In August 2016 Mr T turned 60 and drew his benefits from the transferring scheme. It later transpired that because he was drawing his benefits when the bulk transfer took part, he could no longer take part in it.

7.3 Mr T complained that had he been given clear, full and timely information from his last employer about the terms of the bulk transfer he would have deferred his retirement in order to take part in the transfer. Mr T argued that the employer was under a "moral and ethical obligation" to have provided him with information both about his retirement options (i.e. his ability to defer his pension which was an option he claimed he was unaware of) and the terms of the transfer, after the terms of the bulk transfer had been known in April 2016.

7.4 The member's complaint was rejected broadly on the following grounds:

- Mr T had the opportunity to understand his retirement options including the ability to delay retirement without the employer having to inform him as such and furthermore, advising Mr T that he would have been better delaying putting his pension into payment goes beyond the scope of an employer's duty;
- The Deputy Pension Ombudsman was not satisfied that Mr T had shown any loss (the employer had provided evidence that the benefits were actuarially equivalent in the long term); and
- Evidence also suggested that even if Mr T had been fully informed about the details of the bulk transfer prior to putting his pension into payment, he would have made the same decision in any event.

7.5 The determination is useful affirmation for employers that a duty on the employer to provide information to members about their pension options will only arise in certain very limited circumstances and that it remains the case that employers are not under a duty to provide advice to their employees about valuable pension benefits.

8. CIVIL PARTNERSHIP (OPPOSITE-SEX COUPLES) REGULATIONS 2019

8.1 The Civil Partnership (Opposite-sex Couples) Regulations 2019 were made on 5 November 2019 and came into force on 2 December 2019. The purpose of the regulations is to allow two people who are not of the same sex to form a civil partnership in England and Wales.

8.2 While trustees will need to consider whether any changes are needed to their pension scheme's rules as a result of the regulations, many may find that the changes flow through automatically.

9. ON THE HORIZON

HMRC's GMP equalisation guidance

HMRC had intended on publishing guidance in December 2019 on the tax issues caused by GMP equalisation. We understand that the guidance will not cover equalisation through GMP conversion as "*the issues are proving more complicated to resolve and we continue to explore these*". The guidance will be high-level only and is awaited.

Budget

The Chancellor of the Exchequer, Sajid Javid, has announced that the Budget will take place on Wednesday 11 March 2020.

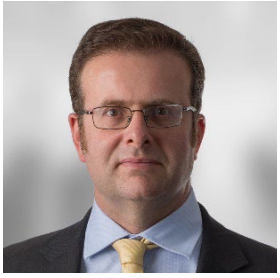
Pension Superfunds

The Governments response to its December 2018 consultation on defined benefit consolidation vehicles (so-called 'pension superfunds') remains outstanding. While a response was expected in December 2019, this was delayed as a result of the December 2019 general election.

Pensions Regulator to consult on a new single code of practice

In July 2019 tPR announced its intention to review its codes of practice and combine them into a single, shorter code. Consultation on the code was delayed as a result of the December 2019 general election and it is now expected in early 2020.

CONTACTS



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