SQUIRE PATTON BOGGS

#PensionsTensions: New Dimensions

Part Five: Legal and Regulatory

Introduction

Welcome to the latest phase of our #PensionsTensions campaign, exploring the current challenges faced by trustees and sponsoring employers of occupational pension schemes. Effective risk management is undoubtedly the key to running a pension scheme well and is the dominant theme in The Pensions Regulator's (TPR's) draft single code of practice. Each factsheet in this series sets out our top "red risks", as well as some mitigation tips and a #PressureMeasure that shows whether we think the pressure on trustees and sponsoring employers is increasing or decreasing. Each factsheet assumes that there is an established risk management system on which additional measures can be built. Do not forget to check our timesaving tip!

In this factsheet, we examine the key risks associated with the many legal and regulatory changes that are expected to come into force during the next year or so.

Comment

Trustees and sponsoring employers already spend considerable time and effort to ensure they achieve the objective of paying the correct benefits to the correct members, at the correct time whilst complying with their trust and regulatory obligations. Even so, evolving regulation could have a fundamental impact on how they do so.

New TPR Powers

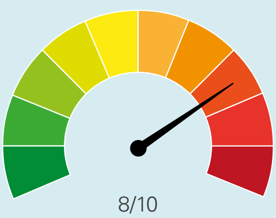
The increased powers given to TPR under the Pension Schemes Act 2021 are intended to enable it to take fast, proportionate action to protect savers and act as a deterrent to those who might put pensions savings at risk. Addressing the potential detrimental impact of corporate activity on pension schemes is the main focus of these new powers. In brief, there will be two new grounds for issuing Contribution Notices, new criminal offences, increased civil penalties (including fines of up to £1 million), two new notifiable events and wider inspection and interview powers. There may need to be a new openness between sponsoring employers and trustees about proposed corporate activity so that both parties can take any necessary actions to avoid attracting enforcement action by TPR. Commercial sensitivities and confidentiality issues will need to be overcome. Given the potentially wide and retrospective nature of regulatory intervention, we expect to see consideration of the benefits and risks of seeking clearance re-emerging as a precautionary measure, with the consequential impact on a deal's timetable and process.

One of the new criminal offences has caused particular concern – that of conduct risking accrued benefits. The deliberately broad wording could potentially catch all manner of corporate and pension scheme activities. In consultation, TPR has stressed that it will take an appropriate and proportionate approach and that in order to secure a prosecution, there would need to be intent, a materially detrimental impact and no reasonable excuse for the conduct. Even so, trustees, sponsoring employers and those with reporting obligations need to understand the new requirements and ensure they can comply.

Tax

The March 2021 budget had to resolve the tension between filling the hole in the Treasury's finances left by pandemic support whilst also avoiding tax changes having a negative impact on consumer spending. Whilst this time around the chancellor's pension tax changes were limited, the prospect of cuts to pensions tax relief as a way of raising tax revenue remains a risk when the government's finances have rarely been so stretched. The freeze in the lifetime allowance until April 2026 could result in increasing numbers of scheme members facing a tax charge on their pension savings in excess of the frozen lifetime allowance, particularly if rising inflation materially increases the value of their pension savings. Trustees should be aware of the potential impact on scheme members and consider what action may be needed to ensure communications and administrative practices reflect the correct tax position.

#PressureMeasure: Legal and Regulatory



With the impact of new legislation, evolving regulatory policies and Brexit, pressure remains high.

Guarantee Enforceability

Brexit has had an impact on the recognition and enforcement of guarantees and other security provided by EU companies to the trustees of UK pension schemes. Reciprocal recognition and enforcement of judgment arrangements between the EU and the UK ceased on 31 December 2020 and there is still uncertainty about how this might be resolved. This means that trustees might incur difficulty in seeking to enforce a guarantee or other security given by an EU company. For example, they might need to have the whole matter re-heard in the courts of the relevant EU member state. If trustees rely on such a guarantee or other security given by an EU company, they should seek advice.

Member Guidance

A consultation by the Financial Conduct Authority in 2020 raised concerns about whether the information provided to pension scheme members by sponsoring employers and trustees of pension schemes could amount to regulated activity where it included comparisons that might steer a member to a particular course of action. This created uncertainty about the use of modelling tools offered to members illustrating retirement options. The response to the consultation was published on 30 March 2021 and included a guide for sponsoring employers and trustees, which provides useful examples of what is likely to be regulated activity and what is not. In addressing the communication challenges highlighted in part one of this #PensionsTensions series, trustees should ensure they correctly draw the line between providing information and giving advice.

Clear Legal Obligations

Parts three and four in this #PensionsTensions series considered tensions around paying the correct benefits, with appropriate governance rigour. That is trickier to achieve where legal documentation is not clear and accurate, particularly as schemes move closer to their eventual destination. There is more likely to be a disconnect where there are multiple deeds of amendment. Trustees can better manage documentary risk, including any legal and in practice mismatch in their benefit obligations, by ensuring their archives of important documents, including current and historic scheme rules, are up to date and easily available. Trustees could consider consolidating trust deeds to bring together rule changes and preparing benefit specifications and balance of power summaries, each to support their trustee knowledge and understanding of key scheme documents and to assist operational efficiency and legal compliance.

Red Risk Flags

- Is it clear who is responsible for carrying out any notification requirements, particularly in relation to employer notifiable events?
- Are pension scheme impacts embedded into the sponsoring employer's decision-making processes, and are its pension objectives clear?
- Can the trustees substantiate their reliance on a guarantee or other security?
- Are there multiple deeds of amendment that have not been consolidated?

Mitigation Tips

- Undertake training on the increased powers of TPR and include representatives of the sponsoring employer with responsibility for the pension scheme.
- Seek advice on any Brexit impact on guarantees and PPF eligibility.
- Review member communications and tools to ensure they provide information, not advice.
- Consider consolidation of trust deeds and rules, and preparation of a complete scheme bible

What the Regulator Says

Extracts from a speech by David Fairs, at the Outer Temple webinar on 30 March 2021 (the entire speech can be found on TPR's website), include:

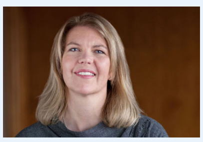
"It's important to appreciate that the new powers we have been afforded are part of a strong package of measures to strengthen our regulatory grip and the options available to us, but they are not going to turn us into a belligerent law enforcement agency or the 'Pensions Police'."

"In short, if you are doing the right thing you have little to worry about."

Time-saving Tip

Build a legal and regulatory review into your business plan to ensure you are ready for anything that could delay or even derail your pension strategy.

Key Contacts



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