



Those who have worked in the pensions industry for a number of years will know that pensions law does not remain static for long. The latest instalment comes in the form of the white paper from the Department for Work and Pensions (DWP), “Protecting Defined Benefit Pension Schemes”, which was issued on 19 March 2018. The paper clarifies the direction of travel in a number of areas, most of which will first be subject to consultation and further legislation, before we have the full picture.

Are we facing a period of steady evolution or an out-and-out pensions revolution? Our series of communications and seminars over the next few months on the changing world of pensions will feature our (R)evolution theme, and we will explore whether the change, and the pace of it, is appropriate.

The Pensions Regulator

In the white paper, the DWP announced that The Pensions Regulator (TPR) will be given increased powers to make it “clearer, quicker and tougher”, including:

- Punitive fines for those who deliberately put their pension plan at risk
- The introduction of criminal offences for those found to have committed wilful or grossly reckless behaviour in relation to a defined benefit (DB) pension plan
- Greater powers of investigation, including the ability to compel individuals to submit to an interview
- A strengthening and widening of the notifiable events and clearance regimes

The government intends to introduce requirements for sponsoring employers or parent companies, in consultation with trustees, to make a “statement of intent” before certain business transactions take place, stating that they have appropriately considered the impact on any affected DB plan and setting out how they propose to mitigate any detrimental impact. There will be some corporate concern that the need for such a statement may compromise confidentiality and potentially unduly restrict normal corporate activity, but the government is to work with TPR to determine its approach and to ensure that only those business transactions “which pose the highest potential risk” will be in scope. There was some speculation that the current voluntary clearance system might become mandatory, but the government seems to be steering clear of this approach to avoid an adverse effect on legitimate business activity, which will be a relief to the corporate world.

DB Funding

TPR will consult on a revised code of practice, which will focus on:

- How “prudence” is demonstrated when assessing pension plan liabilities
- What factors are “appropriate” when considering recovery plans

TPR is concerned that some trustees are focusing on short-term (inter-valuation) outcomes rather than agreeing long-term objectives with the employer when setting the statutory funding objective. TPR will produce guidance on setting long-term objectives, taking into account the pension plan’s circumstances.

Legislation requiring compliance with “clearer funding standards” will be brought into force “at the earliest opportunity” and TPR will be given additional powers to enforce these standards. We would urge TPR to seek to clarify boundaries rather than be too prescriptive in terms of funding standards. The scheme-specific nature of the current funding standard seems to work well on the whole, and the last thing that the pensions industry needs is anything resembling a return to the Minimum Funding Requirement.

The DWP does not believe that there is a general affordability problem with DB pension plans, but it acknowledges that there are perceptions (possibly created by a lack of understanding of the various funding standards) that DB pensions are in crisis. TPR will produce a factsheet explaining the main ways of measuring pensions assets and liabilities for the benefit of “members, journalists, commentators and the general public”. We suspect that this will not be sufficient to stop sensationalist headlines from pockets of the media, but it may help to quell some of the alarm that arises from such news reports.

Chair of Trustees

DB plans will be required to appoint a chair of trustees (if they do not have one already) and a chair's statement reporting on key scheme funding decisions will need to be submitted to TPR alongside the triennial valuation. The content of the statement is yet to be decided, but it may also include comment on how trustees will meet key governance standards and achieve value for money from their running costs and investment decisions – thus having broad parallels with the annual governance statement for pension plans with defined contribution (DC) benefits. The government observes that more needs to be done to promote greater transparency of costs and charges in DB pension plans, as this is a key part of good governance, although efficiencies are unlikely to transform materially a pension plan's funding position.

Consolidation

At the end of 2018, consultation will take place on proposals for changes to the legislative framework and authorisation regime to allow new consolidator DB plans to enter the marketplace, including commercial consolidator vehicles. At the same time, the DWP will work with TPR to raise awareness of the benefits of consolidation, which, according to its evidence, are greater economies of scale, better investment opportunities and higher quality governance in comparison with smaller pension plans. Of course, consolidation is not just about what current or future legislation will allow; it is also about trustees believing that consolidation achieves the best outcome for pension plan members – which is a very difficult assessment. Although the DWP will encourage trustees to consider consolidation as an option, it will not be appropriate for all pension plans.

It will be a very difficult task for the DWP to come up with a framework for commercial consolidator vehicles that is commercially viable, whilst at the same time providing adequate protection for members and not posing an unacceptable risk to the Pension Protection Fund. The white paper foresees options where consolidation would, for a price, sever the link with the original sponsoring employer; other options may involve some form of ongoing employer attachment. The new structures are likely to require a high level of supervision from TPR, with stricter funding standards and the injection of a suitable amount of risk capital from those who are ultimately able to profit. What funding criteria will have to be met before profit can be extracted from a commercial consolidator? What is a "surplus" for this purpose? By the time that commercial consolidator arrangements become a reality, TPR will at least have the experience of implementing the DC master trust framework, which has some parallels (although from a funding perspective it is a different beast entirely).

Setting aside legislation and commercial practices for a moment, the reaction of pension members to being put in a consolidator vehicle that has no link with their current or former employer, and mitigating the risk for trustees to enable them to transfer liabilities to such a vehicle, will be separate hurdles to overcome. Most employees have trust in their employer but will not necessarily have trust in an arrangement that will sever links with their employer and the trustee body. Some pension arrangements have a complicated benefit history (due to mergers, different benefit categories, etc.) and there is a wealth of knowledge within the trustee body, the employer, the administrators and the advisers – there will be a (not unreasonable) fear that this knowledge will be lost on consolidation and new risks will be created.

Employer Debt

The employer debt legislation for multi-employer pension arrangements has been revised a number of times since 2005. A new "deferred debt" arrangement came into force on 6 April, designed to help employers trapped in non-associated multi-employer pension plans, many of whom are unincorporated sole traders and family businesses and where many of the plans are "last man standing". The plumbing industry pension arrangement is a case in question, where sole traders would often enrol their apprentices and years later become liable for substantial debts.

The new legislation will allow employers to defer the debt, subject to trustee agreement, but it does not cap their liability under a "last man standing" plan; whilst they are statutory employers, their liabilities are likely to continue to grow. The outcome is harsh for sole traders who followed industry practice at the time in terms of pension provision and are now faced with liabilities that affect their personal wealth. However, other solutions may involve reducing member benefits, which is also unpalatable. The employer debt system continues to be a slow evolution rather than anything representing revolution. We suspect that there will be further developments.

RPI/CPI

This is one issue on which we now have greater clarity on likely legislative intervention. The government has confirmed that it does not currently intend to amend legislation to give trustees or employers a specific power to change the measure of inflation from RPI to CPI for revaluation and pension increases in circumstances where plan rules do not allow this. This issue has been the subject of debate since 2010 when the Coalition government first announced its intention to change the index used in the annual revaluation order from RPI to CPI – this had the effect of creating an indexation lottery for private sector pension plans where the outcome depended on the precise wording of the pension plan rules. A number of trustees and employers have applied to the courts for clarification of their rules to ascertain whether a change of index is permissible. The introduction of overriding legislation for this purpose would have created a precedent that many in the pensions industry would have found unsettling, although some sponsoring employers with underfunded DB plans may have been hoping for a different outcome. This remains a "live" issue for many pension plans where recent case law could affect the extent to which a change of index is possible.

More (R)evolution to Come

Look out for further communications under our Pensions (R)evolution banner. We will consider some of these themes in more detail in our forthcoming series of pensions breakfast seminars, "The Pensions (R)evolution – The Pace of Change".

Our Relationship With the Pensions Management Institute

We are delighted to announce that we are teaming up with the Pensions Management Institute (PMI) as an Insight Partner. PMI's Insight Partnerships are developed exclusively with organisations considered to be thought leaders and experts in the industry, to support innovation on current and pertinent issues and to add value through the delivery of insight.

Gareth Tancred, Chief Executive of PMI, commented, "Navigating the legal and regulatory landscape is a key concern for our members. Squire Patton Boggs is not only a key player in law, but also active in seeking to influence government policy both here in the UK and worldwide, making them ideally placed to provide our members with the latest industry thinking. We look forward to working with Squire Patton Boggs to provide specialist support to our members."

See our [press release](#) for more details.

As part of our Insight Partnership with PMI, we will also be hosting [complimentary legal consultations](#) at the Pensions Aspects Live conference on Thursday 19 April 2018. If you plan to attend the conference, why not register your interest and come along to see us?

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