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The Pensions Regulator: powers to protect pension benefits

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Summary

The Pensions Regulator (TPR) has 'anti-avoidance' powers which it can use with the aim of protecting benefits in defined benefit (DB) pension schemes (i.e. schemes which provide benefits based on salary and length of service) and the Pension Protection Fund.

The Regulator's two main 'anti-avoidance' powers are to issue:

- Contribution Notices - which require a target to make a lump sum payment to a scheme (or to the Pension Protection Fund);
- Financial Support Directions, which require the target to put arrangements in place to support the scheme, the details of which are approved by the Regulator.(see The Pensions Regulator– anti-avoidance powers.).

A clearance procedure is available for those wishing confirmation that they will not be subject to such powers when dealing with events that may impact upon their pension scheme, such as a business transaction.

In its December 2016 report on DB schemes, the Work and Pensions Select Committee recommended that reforms should enable TPR to intervene sooner when difficulties become apparent. It recommended that the Government should consult on new rules for situations where TPR clearance of major corporate transactions would be mandatory and that TPR should be able to impose punitive fines that could treble the amount payable under TPR's existing anti-avoidance powers (press release, 21 December 2016).

In its February 2017 Green Paper, Security and Sustainability in Defined Benefit Pension Schemes, the Government said that the "overarching view of virtually all stakeholders is that the regulatory regime for DB pensions is satisfactory" but that there might be a case for "limited changes to the regulation of DB provision to help employers and trustees manage liabilities more effectively in some of the circumstances that exist" (para 139-40). It asked for views on reforms that had been suggested, including:

- Proactive compulsory clearance of certain corporate activities in limited circumstances;
- Levying substantial fines on companies for corporate transactions which have a detrimental impact on schemes; and
- Widening the criteria for Regulatory Apportionment Arrangements.

In its March 2018 White Paper, the Government said it would strengthen the regulatory framework and the Regulator's powers to:

1. Give the Regulator powers to punish those who deliberately put their pension scheme at risk by introducing punitive fines;

2. Legislate to introduce a criminal offence to punish those found to have committed wilful or grossly reckless behaviour in relation to a pension scheme and, build on the existing process to support the disqualification of company directors; and

3. Work with the Regulator to strengthen the existing notifiable events framework and voluntary clearance regime so that employers have appropriate regard to pension considerations in any relevant corporate transactions. This includes improving the effectiveness and efficiency of the Regulator's existing anti-avoidance powers. We will work with relevant parties to ensure that these measures do not have an adverse effect on legitimate business activity and the wider economy.

4. Legislate to give the Regulator some of the information-gathering powers already in place for automatic enrolment and Master Trusts to its Defined Benefit and Defined Contribution functions, including the power to compel any person to submit to an interview, the power to issue civil sanctions for non-compliance and an inspection power. (Cm 9591, chapter 1).

A further consultation on Protecting DB pension schemes – a stronger Pensions Regulator was published in June 2018, with a government response in February 2019.

The *Pension Schemes Bill [HL] 2019-21* contains provisions intended to help TPR to meet their aim of being "clearer, quicker and tougher" and afford increased protection for Defined Benefit scheme members' savings." They relate to:

- **Criminal and civil sanctions –** strengthening the existing sanctions regime by introducing three new criminal offences and a new power to issue civil penalties of up to £1 million.
- Changes to the regime for **Contribution Notices** (one of the powers available to TPR to 'recover any losses caused to a Defined Benefit pension scheme as a result of avoidance behaviours').
- **Corporate transaction oversight –** provisions in the Bill would 'require persons involved in a corporate transaction to make a statement setting out information about the event and how any detriment to a Defined Benefit pension scheme, as a result of this event, is to be mitigated.'
- Provisions to give TPR a 'more coherent set of **information gathering powers**.' (Explanatory Notes, paras 13 to 23).

When the Bill was in the Lords, Peers expressed concern that the scope of clause 107 (sanctions for avoidance of employer debt) was too wide (potentially relating to could inject "great uncertainty into pensions administration" and have the effect of deterring "ordinary pensions and business activity." The Government responded that the aim was to "target individuals who intentionally or knowingly mishandle pension schemes or endanger workers' pensions by behaviours such as chronic mismanagement of a business or avoiding pension liabilities." It was important that "where the elements of an offence are met, no matter who has committed it, the regulator should be able to respond appropriately. Any restriction of the persons potentially in scope would create a loophole for those people to act in such a way" (HL Deb 30 June 2020 c634-8).

Third Reading in the Lords is scheduled for 15 July 2020.

1. Overview

A Defined Benefit (DB) pension scheme promises to pay a pre-determined amount of pension to its members based on their salary and years of contribution.[1]

1.1 *Pensions Act 2004*

A number of high-profile cases of schemes winding up under-funded on the insolvency of the employer, led the Labour Government to introduce a number of measures in the Pensions Act 2004, aimed at improving the protection of pension scheme members' benefits and making provision easier for employers. One of these was the establishment of a new Pensions Regulator (TPR) to replace the previous Occupational Pensions Regulatory Authority (OPRA).[2]

The legislation previously in force had led OPRA to direct its effort towards "high volumes of relatively low value reports and breaches." In contrast, TPR would take a "risk-focused and proactive approach."[3]

It would also have a significantly wider range of powers and responsibilities.[4] While OPRA had no power to act against employers' attempts to avoid meeting their pension obligations, and no duty to do so, TPR would have a regulatory tool kit, enabling it to take a targeted approach to protecting pension scheme members.[5]

The 2004 Act also established the Pension Protection Fund (PPF) to provide compensation to members of eligible defined benefit (DB) pension schemes which wind up underfunded on the sponsoring employer's insolvency. The Government recognised that this created 'moral hazard': i.e. that unscrupulous employers might seek to side-step their responsibilities to a scheme and off-load it onto the PPF.[6] The then Pensions Minister, the late Malcolm Wicks, explained that mitigating this risk was "one of the biggest challenges" the Government faced in introducing the PPF" but one that needed to be addressed to "safeguard the integrity and sustainability of the fund and avoid placing an unfair burden on levy payers." [7]

1.2 Regulator's powers

The Government recognised that the PPF created different forms of moral hazard. The legislation already included provision to address some of them – for example, a cap on compensation for those under normal

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1 DWP, Security and Sustainability in Defined Benefit Pension Schemes, February 2017, p13
2 Library Briefing Paper RP 04/18 Pensions Bill (Feb 2004); *Pensions Act 2004,* Part 1
3 DWP, 'Simplicity, security and choice, working and saving for retirement: action on occupational pensions', June 2003, Cm 5835
4 The Pensions Regulator, 'Annual report and accounts, 2005-06', p3
5 DWP, 'Simplicity, security and choice. Working and saving for retirement. Action on occupational pensions', 2003; NAO, 'The Pensions Regulator: Progress in establishing its new regulatory approach', HC 1035, Session 2006-07, 26 October 2007
6 See Library Briefing Paper SN-03917 Pension Protection Fund (April 2016)
7 SC Deb, 27 April 2004, c768

pension age would avoid "potential perverse incentives for key decision makers to allow companies to go into insolvency."[8]

At Commons Committee Stage, Malcolm Wicks announced the introduction of powers for TPR to issue Contribution Notices and Financial Support Directions. These would help to mitigate:

> […] the risk posed by unscrupulous employers who might seek to use company structures and business transactions as a cover for side-stepping their pension obligations in the form of the debt due from the employer under section 75 of the *Pensions Act 1995*.[9]

Financial Support Directions could also be used in other circumstances in which "as a result of actions that may well have been perfectly legitimate and not aimed at avoiding pension liabilities, schemes end up with a participating employer who is financially weak and unable to meet its pension liabilities."[10]

Mr Wicks explained that the provisions would be operated and enforced by TPR, working closely with the PPF:

> The powers will need to be exercisable by the regulator, as the very nature of the actions that they are designed to capture is such that manipulation may occur some time before the PPF would normally get involved in a scheme as a result of an employer insolvency. Moreover, the pensions regulator will have the intelligence and expertise, as a result of its day-to-day work monitoring pension schemes, to deal proactively with the risks of moral hazard.[11]

The then Shadow Pensions Minister, Nigel Waterson said that such 'anti-avoidance' provisions were "necessary, and we do not argue with the need for them."[12]

1.3 TPR's process

A decision to issue a Contribution Notice, Financial Support Direction must be made by the determinations panel of the Pensions Regulator.[13]

TPR explained the process in evidence to the Work and Pensions Committee in 2016:

> We will undertake a comprehensive investigation to determine whether it is appropriate and reasonable to exercise either of these powers. These investigations are complex and can involve the review of thousands of documents and other pieces of expert and witness evidence. When we are satisfied it is appropriate to use a power we will issue a Warning Notice to the proposed targets and any other directly affected parties.
>
> The investigating team do not determine whether a power is exercised. This decision is made by our Determinations Panel, an independent committee which has no connection to the people undertaking the investigation. The Determinations Panel hears the

8 SC Deb, 27 April 2004, c768
9 Ibid
10 Ibid c780`
11 Ibid; Memorandum of Understanding between DWP, PPF and TPR, February 2008
12 Ibid c771
13 *Pensions Act 2004*, s9-10, Sch 2

> case and representations from the proposed targets, and will determine if it is reasonable to exercise the power.
>
> We can issue a Contribution Notice in relation to acts up to 6 years prior to when we issue a Warning Notice.
>
> We can issue a Financial Support Direction where a connection/association to the scheme sponsor has been in place within 2 years prior to TPR issuing a Warning Notice. We can consider, as part of our assessment of whether or not it is reasonable to exercise the power, any acts or events which have taken place during the proposed targets' connection/ association with the scheme sponsor, and there is no time limit on how far we can look back.
>
> Generally speaking, the fact a company has moved into insolvency does not impact the use of our avoidance powers, and we have used our powers on a number of occasions in which the employer has become insolvent.[14]

See also Determinations Procedure on TPRs website.[15]

1.4 Debate

A report by the National Audit Office in 2007 found that TPR had made sparing use of its powers, preferring to concentrate on education and influence:

> 4.17 TPR was given much greater enforcement powers than those of the previous regulator. To date it has used education and enablement in preference to enforcement. It has not yet felt the need to use its enforcement powers widely considering it more proportionate to use the threat of powers to influence the desired behaviour. In particular TPR believes the threat of a Contribution Notice or a Financial Support Direction has resulted in increases in the funding of pension schemes that are part of a corporate transaction.[16]

An article by a pensions lawyer in 2014, noted that cases in which TPR's formal powers had been used remained the exception rather than the rule. TPR had shown a willingness to use its powers but had not "held corporate activity hostage".[17]

The fate of BHS Pension Scheme, in particular, gave rise to questions about TPR's powers and the extent to which it used them.[18] In a December 2016 report, the Work and Pensions Select Committee concluded that TPR had a mixed record:

> **145. Under TPR's existing anti-avoidance powers, an employer seeking to avoid its responsibilities to a pension scheme may well take a punt on risking enforcement action. TPR has a mixed record, resolution may take several**

14 Written Evidence to the Work and Pensions Select Committee (PPF0004, May 2016)
15 The Pensions Regulator. Determinations panel. Procedures for cases
TPR website – determinations procedure; See 'The Pensions Regulator. Determinations Panel Procedure', (revised June 2008)
16 National Audit Office, 'The Pensions Regulator: Progress in establishing its new regulatory approach', HC 1035 Session 2006-07, 26 October 2007
17 'Comment – The regulator's powers have not held corporate activity hostage, *Pensions expert,* May 2014
18 'UK regulator urged to be 'robust' on the pensions before BHS collapse', *Financial Times,* 2 may 2016

> **years, and the most TPR might hope to recover is the amount of support the employer should have provided to the scheme in the first place. In the meantime, the pension scheme members are left in limbo.**[19]

It recommended that the Government consult on:

- Giving TPR powers to add 'punitive fines' to Contribution Notices and Financial Support Directions; and
- Proposals to require advance clearance from TPR for certain corporate transactions that could be materially detrimental to the funding position of a DB scheme.[20]

1.5 February 2017 Green Paper

In its February 2017 Green Paper Security and Sustainability in Defined Benefit Pension Schemes, the Government said that the "overarching view of virtually all stakeholders is that the regulatory regime for DB pensions is satisfactory." However, there might be a case for "limited changes to the regulation of DB provision to help employers and trustees manage liabilities more effectively in some of the circumstances that exist."[21] It asked for views in relation to a range of changes which had been suggested, including:

- Proactive compulsory clearance of certain corporate activities in limited circumstances;
- Levy substantial fines on companies for corporate transactions which have a detrimental impact on schemes.
- Require sponsors to engage with and provide information to trustees in a timely manner.
- Require consultation with trustees before paying dividends if scheme is severely underfunded.
- Better communications with members.[22]

On 11 January 2018, Pensions Minister Guy Opperman said a White Paper would be forthcoming later this Spring.[23]

Section 2 below discusses TPR's powers, how they have been used and proposals that have been made for change.

A recommendation to consider additional scheme funding powers is discussed in CBP 4877 Pension Scheme Funding requirements (October 2017).

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19 Work and Pensions Committee, Defined Benefit pension schemes, December 2016
20 Ibid, para 141-6
21 DWP, Security and Sustainability in Defined Benefit Pension Schemes, Cm 9412, February 2017, para 139-40
22 DWP, Security and Sustainability in Defined Benefit Pension Schemes, Cm 9412, February 2017, para 139-40 page 73
23 HC Deb 11 January 2018 c586

1.6 The March 2018 White Paper

On 22 January 2018, following the collapse of Carillion, Shadow Work and Pensions Secretary Debbie Abrahams asked why the Government had not acted earlier:

> Yesterday, the Prime Minister chose to announce via the media, in part in response to the collapse of Carillion, that the Government planned to introduce tough new rules to stop private sector pension abuse.[…] Given the severity of the financial problems facing Carillion, why did the Government not act then, rather than attempting to close the stable door after the horse had bolted?[24]

Work and Pensions Secretary Esther McVey said the Government had been consulting on measures to strengthen TPR's powers and would set out proposals in its forthcoming White Paper.[25]

The White Paper published on 19 March 2018 said that for the "small number of employers evading their obligations", the Government would "put in place tougher, more proactive powers so that the Pensions Regulator can intervene more effectively to protect individuals." It would:

> Strengthen the regulatory framework and the Regulator's powers, as set out in the Government's 2019 manifesto, to:
>
> - Give the Regulator powers to punish those who deliberately put their pension scheme at risk by introducing punitive fines;
> - Legislate to introduce a criminal offence to punish those found to have committed wilful or grossly reckless behaviour in relation to a pension scheme and build on the existing process to support the disqualification of company directors; and
> - Work with the Regulator to strengthen the existing notifiable events framework and voluntary clearance so that employers have appropriate regard to pension considerations in any relevant corporate transactions. This includes improving the effectiveness and efficiency of the Regulator's existing anti-avoidance powers. We will work with the relevant parties to ensure that these measures do not have an adverse effect on legitimate business activity and the wider economy. [26]

Responses

Shadow Pensions Minister Jack Dromey described the White Paper as a missed opportunity to "properly tackle the widespread problems facing DB schemes."[27]

The Work and Pensions Select Committee welcomed the fact that some of its recommendations for "nuclear deterrent" fines had been taken

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24 HC Deb 22 January 2018 c28
25 Ibid para 25-6
26 DWP, Protecting Defined Benefit Pension Schemes, Cm 9591, March 2018
27 'Shadow Minister: The White Paper has been a long time coming and is a missed opportunity', *Professional Pensions,* 26 October 2017

forward but said pension rights were still at risk while the Government consulted:

> Although the White Paper appears to leave room for the deterrent fines to be applied immediately – another very welcome move - the legislation needed to enact the new regime in full will not happen before 2019-20 at the earliest. In the meantime, with Government proposing to consult further, pension rights are still at risk from unscrupulous businesses seeking to avoid their pension obligations.[28]

Chair of the Committee Frank Field said there had to be a credible threat of TPR's powers being "deployed in full and at speed."[29]

The Pensions Regulator welcomed new proposals to improve its ability to intervene to protect pension savers:

> We called on government for more effective powers and so we welcome the proposals.
>
> Planned improvements to our scheme funding, information-gathering and anti-avoidance powers will enable us to be clearer about what we expect from employers in relation to scheme funding and tougher where a scheme is not getting the funding it needs.
>
> Furthermore, strengthening the notifiable events framework will improve our regulatory grip and will ensure we are sighted sooner on planned transactions that could pose a risk to scheme members.
>
> We will now work closely with government to develop the White Paper's proposals, including fines and criminal sanctions, to ensure they are proportionate, act as an effective deterrent and work in practice.
>
> The best support for a DB scheme is a strong employer and we believe the current flexible funding framework, which allows employers to balance growth with meeting pension benefits, remains the right approach and we will aim to retain this flexibility in any new approach.[30]

1.7 The regulatory strategy

In May 2018, TPR published its plans for taking a "clearer, quicker and tougher approach to driving up standards in the pensions sector." On effective regulation of DB, it said:

> We are committed to regulating as effectively as possible, so that members of DB schemes receive the benefits they are entitled to at retirement. We will focus particularly on the schemes that present the biggest risks and take action where funding is not appropriate for that scheme or against those who are seeking to avoid their liabilities.
>
> We will continue to assess the DB landscape to highlight trends and respond to issues by setting out clear expectations of schemes through our DB landscape and Annual Funding Statement

28 Pensions still at risk while Government continues to consult, Work and Pensions Select Committee, 19 March 2018
29 Ibid
30 TPR welcomes proposed new powers to protect pension savers, the Pensions Regulator, 19 March 2018

> publications. We will seek to maximise good outcomes for all DB scheme members and demonstrate clear measures in achieving that aim.
>
> As part of developing a broader reach and a more segmented risk-based approach, we will be focusing further on smaller DB schemes. Alongside this work, we will continue to engage proactively with larger schemes, making sure we are clear about our expectations of trustees in their specific circumstances. If we see a situation where we believe a scheme is not being treated fairly relative to other creditors, we are likely to intervene and if necessary use our formal powers.
>
> We will continue to work closely with the DWP in implementing the recommendations of the DB White Paper, making revisions to our DB funding code, regulatory policy and practices where necessary.

On 19 March 2018, the Pensions Regulator and Financial Conduct Authority published a call for input: regulating the pensions and retirement income sector: our strategic approach.

They published a joint regulatory strategy on 18 October 2018. Among the risks identified were: consumers receiving lower levels of retirement income due to underfunding of DB schemes and money being lost through governance and administration errors. [31] To address this, TPR proposed:

> - Starting one-to-one managed supervision with an initial group of DB schemes and implementing a range of regulatory tools sot that more DB schemes will experience TPR intervention around their initial valuations and reduction of deficits
> - Supporting DWP in implementing the policy intentions of the recent DB White Paper – including new powers for TPR, new codes of practice for trustees and employers and new authorisation and supervision frameworks for DB consolidators.[32]

Another area of risk identified was transfers out of DB schemes into DC schemes. This is covered in Library Briefing Paper CBP-8382 Pension freedoms and 'safeguarded benefits' (August 2018).

1.8 Consultation on TPR's powers

In June 2018, the Government launched a consultation on proposals to improve the Pensions Regulator's powers so that they can:

- Be more proactive and get involved earlier when employers make changes which could affect the pension scheme;
- Obtain the right information about a scheme and its sponsoring employer;
- Get redress for members if things go wrong.

The proposed improvements included:

[31] FCA and TPR, Regulating the pensions and retirement income sector: our joint regulatory strategy, October 2018, p8

[32] Ibid, p14

- Clearer funding standards for all pension schemes, together with measures to help employers, trustees and the Pensions Regulator work together to better secure the pension promises – these include the requirement for Defined Benefit schemes to have a Chair of Trustees and to prepare and submit a Chair's Statement;
- Greater clarity for employers to help them better understand how and when to notify the Regulator of certain business transactions and events, improving the Regulator's ability to ensure that the needs of the pension scheme are properly considered when companies undertake corporate transactions;
- Enhanced powers for the Pensions Regulator to obtain the right information when they need it;
- New powers to strengthen existing safeguards and to enable the Regulator to deter and, when necessary, punish wrongdoing; and
- New possibilities for scheme consolidation where appropriate.[33]

On 11 February 2019, the Government responded to the consultation and announced its proposals to improve TPR's powers to that they:

- Can be more proactive and get involved earlier when sponsoring employers make changes which could impact the pension scheme;
- Have the necessary powers to be able to obtain the right information about a scheme and its sponsoring employer in a timely manner;
- Are able to gain redress for pension schemes and its members when things go wrong; and
- Can deter reckless behaviours.[34]

It highlighted its intention to introduce two new criminal offences to prevent and penalise mismanagement of pension schemes:

> The first will target individuals who wilfully or recklessly mishandle pension schemes, endangering workers' pensions, by such things as chronic mismanagement of a business; or allowing huge unsustainable deficits to build up; or taking huge investment risks; or a combination thereof. We will introduce a new custodial sentence of up to seven years' imprisonment or an unlimited fine for this offence. This brings the punishment in line with similar offences in financial services.
>
> The second, which will attract an unlimited fine, will target individuals who fail to comply with a Contribution Notice, which is issued by The Pensions Regulator requiring a specified amount of money to be paid into the pension scheme by that individual. We will also introduce a new civil penalty of up to £1 million for this offence.[35]

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33 Protecting defined benefit pension schemes – a stronger Pensions Regulator, June 2018
34 Ibid p5
35 HCWA1319 11 February 2019

Comment

TPR welcomed the proposed new powers which, as a package, would allow it to identify problems earlier and take more effective action.[36]

Some commentators questioned whether the proposed offence of "wilful" or "reckless" behaviour in relation to a pension scheme would be enforceable. Professor Horton of Warwick Business School said:

> Government plans to protect DB pension schemes are a welcome development, but the focus is still on punishing 'reckless' trustees, rather than encouraging CEOs to fund pension schemes properly. It is incredibly difficult to define what constitutes 'reckless'. The decision the trustees took may have been completely rational at the time; they just turned out to be the wrong ones.[37]

She said it seemed more logical to incentivise them to fund the main pension scheme properly by requiring them to be members.[38]

The *Financial Times* was also sceptical, arguing that "it is a high legal bar that could be hard to meet…one or two failed prosecutions would quickly undercut the measure." It was critical of the decision not to pursue mandatory clearance, which it said would have been preferable to leaving it voluntary, even if it slowed mergers and acquisitions. It said legislation on companies' responsibilities remained "weak and muddled."[39]

1.9 *Pension Schemes Bill [HL] 2019/21*

Legislation to strengthen TPR's powers is in Part 3 of the *Pension Schemes Bill [HL] 2019/21.*

The Government says that cumulatively, the measures will help TPR meet its aim of being "clearer, quicker and tougher," and in turn will afford increased protection for Defined Benefit scheme members' savings" The powers relate to:

- Changes to strengthen and update the regime for **Contribution Notices** (one of the powers available to TPR in response to avoidance behaviours) (see section 2.1 below).
- **Criminal and civil sanctions -** strengthening the existing sanctions regime by introducing three new criminal offences and a new power to issue civil penalties of up to £1 million (see section 2.3 below).
- **Corporate transaction oversight –**to "require certain persons involved in a corporate transaction to make a statement setting out information about the event and how any detriment to a

For more information

About the Pension Schemes Bill – see the Parliament website. Library briefing papers on other parts of the Bill are here.

[36] Statement on DWP's announcement regarding new powers for TPR, 11 February 2019
[37] 'Force CEOs to join company DB scheme to prevent reckless behaviour, says study, *Professional Pensions,* 13 February 2019; See also' City experts sceptical of jail terms for pension abuse,' *Financial News,* 11 February 2019; Steve Webb tweet, 10 February 2019
[38] Doubts raised over locking up pension mis-managers, *FT Advisers,* 12 February 2019
[39] 'Securing pensions needs more than jail threats', *Financial Times* editorial, 12 February 2019

Defined Benefit pension scheme, as a result of this event, is to be mitigated' (see section 2.6 below).

- Provisions to give TPR a more coherent set of **information-gathering powers** (see section 2.7 below). This is because the current powers vary depending on the circumstances. "The fact that the Regulator has the power to undertake inspections only in some circumstances, interviews in others, or issue civil penalties in different specified circumstances, can hinder investigations and cause confusion among those being regulated."[40]

Responses

Chief Executive of the Pensions Regulator, Charles Counsell, said that TPR's oversight of corporate transactions would be improved, giving it the opportunity to engage with employers on appropriate mitigations:

> Sponsoring employers or parent companies will be required to provide a declaration of intent to us, copying trustees, evidencing consideration of any impact to the scheme from a proposed transaction and setting out the proposed mitigation, as soon as practicable. The declaration will also need to include details of the communications they have had with trustees on the proposed transaction. We will revise our clearance guidance to make expectations more explicit, with more useful examples.[41]

The provision in the Bill for a new criminal offence and a new civil penalty of up to £1 million, combined with improved avoidance powers, had the potential to act as a strong deterrent. Criminal prosecution would be a high bar, which TPR would only use "in the right circumstances."[42]

The provisions were welcomed by the Pension and Lifetime Savings Association (PLSA)

> We support new powers for the Pensions Regulator to take action sooner, impose significant fines, and have more oversight of risky corporate transactions in order to prevent reckless behaviour and protect savers' hard-earned money."
>
> Cumulatively, the improvements to the regulator's powers outlined in this Bill will help the regulator to meet its aim of being "clearer, quicker, and tougher". In turn, this will afford increased protection for defined benefit scheme members' savings.[43]

A blog-post from a partner at Lane Clarke Peacock said the Bill was set to make "sponsors and trustees considerably more cautious about DB schemes."[44]

Second reading debate

Introducing the Bill's Second Reading debate, Work and Pensions Minister Baroness Stedman-Scott summarised Part 3 of the Bill:

40 *Pension Schemes Bill [HL] 2019/20* - Explanatory Notes, paras 13-23
41 Charles Counsell's speech at Pension Schemes Bill launch event, October 2019
42 Ibid
43 PLSA comments on new Pension Schemes Bill, 14 October 2019
44 New Regulator powers set to make sponsors and trustees considerably more cautious about DB schemes, LCP, December 2019

> It places a requirement on those responsible for corporate transactions to set out in a statement how they will mitigate any adverse effects on the pension scheme. The measures will improve the regulator's information-gathering powers, enabling it to enter a wider range of premises and require individuals to attend an interview. This will boost the regulator's ability to ensure that those responsible comply with pensions legislation. There will also be new civil and criminal sanctions to punish those who wilfully or recklessly harm their pension scheme, including a maximum seven-year prison sentence and a civil penalty of up to £1 million.[45]

Opposition peers raised questions about the level of the penalties but also concerns about the potential scope of the sanctions.[46] Former Labour Work and Pensions Secretary Lord Hutton did not think the case had been made for this extension in powers:

> It is clear that not only is the scope of this new offence much wider than what was originally proposed but it is also very possible that it could operate at a much lower level – criminalising the existing material detriment test, which forms part of the contribution notice regime, and bringing into its net persons associated with scheme management and administration.[47]

Responding to the debate, Baroness Stedman-Scott said that the Government did not want to stop legitimate business activity but needed to "ensure that sufficient safeguards are in place to protect members' pensions from the minority who are willing to put them at risk."[48]

Liberal Democrat Peer Baroness Bowles thought a £1 million penalty would still be too low in some circumstances, given the scale of the deficit revealed in the BHS pension scheme, for example.[49]

The main issues debated at Lords' Committee and Report Stages were whether the scope and level of the proposed penalties.

45 HL Deb 28 January 2020 c1353
46 See, for example, c1367 [Baroness Drake]; and c1386 [Lord Kirkwood]
47 Ibid c1388
48 Ibid c1414
49 Ibid c1371

2. Powers to protect pension benefits

This section looks at how current policy developed, how TPR has used its powers and what proposals have been made for change.

2.1 Contribution Notices

The Pensions Regulator explains…

"Targets of [Contribution Notices] CNs are required to pay cash to a scheme or, in some circumstances, to the PPF.

To issue a CN we must consider that the target was party to an act, or failure to act, that meets one of the following tests:

- 'main purpose' test: one of the main purposes of the act or failure was either to: prevent the recovery of all or part of a debt due to the scheme under section 75 of the *Pensions Act 1995;* prevent such a debt from becoming due, or reduce or compromise that debt
- 'material detriment' test: we consider that the act or failure has detrimentally affected in a material way the chance of accrued scheme benefits being received by or in respect of members

We must also consider that it is reasonable for the target to pay the sum stated in the CN. We will consider any relevant issues, which may include:

- how involved the target was in the act or failure
- the relationship the target had with the employer
- the value of benefits which the target receives or is entitled to receive from the employer

We can start the procedure seeking a CN up to six years after an act, or failure, took place. (TPR website, Anti-avoidance powers)."

How the legislation developed

Section 75 of the *Pensions Act 1995* provides for the calculation of the employer debt to a pension scheme in certain circumstances such as insolvency, the scheme being wound up or an employer withdrawing from a multi-employer scheme.[50]

When the *Pensions Act 2004* was before Parliament, the Government announced that it had decided to give TPR power to issue a Contribution Notice where there was an "act or deliberate failure, a main purpose of which is to prevent the recovery of the whole or part of the section 75 debt."[51] The maximum contribution required would be calculated with reference to the section 75 debt that might otherwise have been recoverable from the employer.[52]

In April 2008, the Government proposed amendments to address concerns about new business models which might "sever the link

50 And *Occupational Pension Schemes (Employer Debt and Miscellaneous Amendments) Regulations 2008* (SI 2008 No. 731)
51 SC Deb, 27 April 2004, c768
52 Ibid

between the employer and the pension scheme in order to operate well-funded occupational pension schemes for profit."[53] It proposed:

- Enabling TPR to issue a Contribution Notice where "the effect of an act is materially detrimental to a scheme's ability to pay members' current and future benefits" (i.e. it would no longer be necessary to prove intent to avoid funding the scheme);
- Removing the provision preventing a Contribution Notice being issued where a party has "acted in good faith, but their actions have had the effect of preventing a debt becoming due." This had proved to be "an unhelpful hurdle which would prevent the powers being used in situations where parties [had] simply not considered the impacts on pension schemes"; and
- Providing that a Contribution Notice could be triggered by a series of acts, not just a single act aimed at avoiding a debt to the pension scheme. [54]

The proposals had a mixed response, with the CBI giving a "cautious welcome" and arguing that it was important not to "ratchet up the regulatory burden" and the TUC saying the changes would "help protect pension schemes against smash-and-grab raids."[55]

Following consultation, the Government announced three filters to the new power:

- TPR would issue a statutory Code of Practice for the circumstances in which it expected to use its power;
- The legislation would include a non-exhaustive list of factors that TPR would be required to consider when determining whether an act or failure to act was "materially detrimental";
- It would not be possible to issue a Contribution Notice where a party had "undertaken due diligence before the act and considered and, where appropriate, mitigated the detriment, and could reasonably conclude that the act would not be materially detrimental."[56]

The amendments to the existing powers were made in the Pensions Act 2008, s126 and Sch 9 and are now in the Pensions Act 2004, ss38-42, as amended.[57] Code of Practice No. 12 - Circumstances in relation to the material detriment test - was published in June 2009.

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[53] DWP Press Release, '14 April 2008 - Increasing protection for pension scheme members – O'Brien'; DWP, 'The powers of the Pensions Regulator. Amendments to the anti-avoidance measures in the Pensions Act 2004,' April 2008, para 2

[54] 'Statement on planned DWP consultation on the powers of the Pensions Regulator', 14 April 2008

[55] 'Regulator will be able to force buy-out firms to fund pensions, *Guardian,* 15 April 2008; TUC Press Release, 18 June 2008, 'TUC calls for full review of buyouts model to safeguard members' interests'; 'Pension regulator gains new powers', *Financial Times*, 15 April 2008

[56] DWP, The powers of the Pensions Regulator. Amendment to anti-avoidance measures in the Pensions Act 2004', April 2008; HL Deb, 27 October 2008, c1432; DWP, 'The powers of the Pensions Regulator. Amendments to the anti-avoidance measures in the Pensions Act 2004', October 2008

[57] Section 126 and Schedule 9; For the debates on the provisions, see Library Briefing Paper SN-02141 Pensions Bill 2007-08 – debates in Parliament (August 2008) (s 7.9).

Some examples of where CNs have been pursued…

In June 2010, the Pensions Regulator determined that a Contribution Notice, for £5 million, should be issued in respect of the Bonas Group Pension Scheme.[58] In June 2011, it announced that it had agreed to settle for £60,000 but commented that this did not signal any change in its approach and that it would not hesitate to use its powers where appropriate to improve the outcome.[59] *Occupational Pensions* commented that the case would have dented companies' respect for the regulator's powers.[60]

In March 2012, TPR set out the action it had taken in relation to the Desmond and Sons Pension Scheme.[61] In May 2015, following a reference to the Upper Tribunal, TPR said the trustees had reached an agreement for contributions to the scheme.[62]

In 2017, the High Court refused an application for judicial review against TPR's decision to issue a second warning notice in relation to the Silentnight Group DB Scheme because there was a procedure for challenging decisions through TPR's Determinations Panel.[63]

As DWP commented in March 2018, contribution notices and financial support directions "have rarely been used so far as, among other reasons, negotiations often led to satisfactory outcomes without the need to take matters further."[64]

Plans to strengthen the CN regime

DWP's June 2018 consultation highlighted some limitations in the legislation:

> Contribution Notices require payment of a cash sum to the scheme. The Regulator must show that the amount sought is "reasonable" when assessed by all relevant factors, which may include the relationship between the target and the employer. However, a recent legal case suggested that Contribution Notices may be limited to the loss caused by the 'act', regardless of whether other circumstances might be thought to make a higher amount reasonable.
>
> Contribution Notices are currently capped at the scheme's section 75 deficit at the time of the 'act'. As there can be many years between an 'act' and recovery under a Contribution Notice, a scheme's deficit could have increased substantially before payment. In addition, the Contribution Notice power does not currently provide any specific mechanism to reflect the range of

58 TPR press release, Regulator confirms Contribution Notice , June 2011
59 Ibid; Report on Bonas case under s89, June 2011
60 Occupational Pensions, 'Regulator in climb-down over its first contribution notice', July 2011
61 TPR Press Release, Regulator publishes details of Contribution Notice case, March 2012
62 Report under s89 in relation to Desmond and Sons, May 2015
63 The Pensions Regulator is successful in legal challenge concerning the Silentnight Group DB scheme, PN 17-02, 12 January 2017
64 DWP, Protecting defined benefit pension schemes, March 2018

> consequences that arise from a delay in the eventual payment in the amount asked for.[65]

DWP proposed changes to strengthen the Contribution Notice regime, including:

- Amending the "reasonableness" test so that there is a stronger focus on the loss or risk caused to a scheme by the 'act' when considering the amount to be demanded;
- Providing a specific mechanism by which impacts of the delay in payment are reflected in the Contribution Notice sum;
- Changing the date on which the cap on the level of a Contribution Notice is calculated (so that it is closer to the final determination, rather than the act);
- Creating an additional limb to the 'material detriment' test, assessed by reference to the weakening of the employer rather than the prospect of scheme benefits being paid many years into the future.[66]

In its response to the consultation in February 2019, DWP said it would proceed with the changesproposed in the consultation document.[67]

Pension Schemes Bill 2019/21

Part 3 of the *Pension Schemes Bill [HL] 2019/21* contains provision intended to strengthen the Contribution Notice regime through greater clarity about the meaning of the existing legislation and enabling TPR to "take effective and efficient action as appropriate."[68]

Clause 103 stems from the proposal in the 2018 consultation to create an "additional limb to the 'material detriment' test, assessed by reference to the weakening of the employer rather than the prospect of scheme benefits being paid many years into the future."[69]

Two new tests - alternatives to the main purpose and material detriment test – would be introduced: i.e.; the "employer insolvency test" and the "employer resources test" and their respective statutory defences:[70]

- The "employer insolvency test" would enable TPR to issue a contribution notice where it was of the opinion that:
  - immediately after an act, or failure to act, the value of a scheme's assets was less than its liabilities; and
  - that if an employer debt under section 75(4) of the *Pensions Act 1995* had fallen due, the act or failure to act would have materially reduced the amount that could be recovered had the employer become insolvent.[71]

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65 DWP, Protecting Defined Benefit Pension Schemes – A Stronger Pensions Regulator, June 2018, page 22
66 Page 23
67 DWP, Government Response to the Consultation on Protecting Defined Benefit Pension Schemes, Feb 2019, p26
68 *Pension Schemes Bill [HL] 2019/20* – Explanatory Notes, paras 17-19 and pp37-42
69 DWP, Protecting defined benefit pension schemes – a stronger Pensions Regulator, June 2018, p23
70 Pension Schemes Bill [HL] 2019/20 – Explanatory Notes, para 104
71 Ibid, para 307

- The “employer resources test” would enable TPR to issue a CN where:
  - the act or failure to act reduced the value of the resources of the employer, and
  - that reduction was material reduction relative to the amount of the estimated employer debt.[72]

2.2 Financial Support Directions

The Pensions Regulator (TPR) explains…

“An FSD [Financial Support Direction] requires the target to put financial support in place for a scheme.

To issue an FSD we must consider that the scheme’s employer was either a service company or ‘insufficiently resourced’ at a time that we choose (known as the ‘relevant time’).

‘Insufficiently resourced’ means that an employer’s resources are valued at less than 50% of its estimated section 75 debt to the scheme at the relevant time. There also needs to be one or more associated or connected entities that have enough value to make up the difference.

We must also consider that it is reasonable to require the target to provide financial support. We consider any relevant issues, which may include similar issues to those we consider for CNs.

We can start the procedure seeking a FSD up to two years after the relevant time.” (TPR website, Anti-avoidance powers).

A Financial Support Direction (FSD) may be issued where the regulator concludes that the sponsoring employer is a “service company or is insufficiently resourced, and it is reasonable to do so.”[73] The use – or potential use – of this power has been used to help ensure that entities connected with or associated with a scheme’s sponsoring employer provide financial support to a scheme when it is reasonable to do so.[74]

When the legislation was before Parliament, the then Pensions Minister, the late Malcolm Wicks, explained:

> There may be circumstances in which, as a result of actions that may well have been perfectly legitimate and not aimed at avoiding pension liabilities, schemes end up with a participating employer who is financially weak and unable to meet its pension liabilities. In particular, that may apply in the case of the debt on the employer imposed under section 75 of the 1995 Act in the event of the scheme winding up or the sponsoring employer becoming insolvent. An example of that is the use of service companies, often as part of entirely legitimate group arrangements. Such entities frequently have no material assets and their sole revenue comes from amounts charged to other group companies for the service of the employees, pursuant to inter-company agreements. If the parent company wishes to dump its pension liabilities, it can simply terminate its agreement with the company and wind both it and the scheme up. The service company will have no assets with which to pay any section 75 debt due. Similarly, the participating employer may, by chance,

72 Ibid para 329
73 TPR issues FSD on Sea Containers Ltd, 6 February 2008
74 Source: TPR; *Pensions Act 2004*, s43 (6)

> be a weak member of the group, equally unable to meet any debt and suitable to be sacrificed by the parent in order to reduce the group's pension liabilities. I am sure that hon. Members will agree that, in general terms, sponsoring employers of pension schemes should be genuine entities carrying on a material trading activity or holding material assets, so that the employer guarantee of the scheme is meaningful.[75]

In response to concerns, the Government provided that the majority of individuals (directors or shareholders) would be excluded from the scope of financial support directions.[76]

Some examples of where FSDs have been pursued…

TPR issued its first Financial Support Directions (FSDs) in relation to Sea Containers Limited (SCL) directing it to provide "financial support for the two pension schemes of its London-based UK subsidiary Sea Containers Services Ltd."[77] On 6 February 2008, following the withdrawal of an appeal to the Pensions Regulator Tribunal, TPR confirmed that SCL would be compelled to provide a form of financial support for the pension schemes within 30 days.[78]

In 2010, TPR's determinations panel determined that FSDs would be issued against companies in the Nortel and Lehman Brothers groups (although in the end they were not issued because each of the cases settled before their references to the Upper Tribunal were determined).

In July 2013, the Supreme Court delivered a judgment to the effect that "liabilities under a financial support direction (FSD) issued against an insolvent company would rank as a provable debt." TPR said that the judgment confirmed that the FSD was "effective in an insolvency". However, it overruled "the findings of the High Court and the Court of Appeal that the costs of complying with an FSD issued against an insolvent target company following insolvency would rank as an expense of the administration or liquidation."[79]

An article in *Insolvency Intelligence* argued that had the Court of Appeal decision not been reversed, the need to take account of pension fund deficiencies elsewhere in the group might have deprived "otherwise-viable members of a corporate group…of any reasonable prospect of survival."[80]

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75 SC Deb, 27 April 2004, cc 780-781

76 DWP Press Release, 'Results of industry consultation on moral hazard clauses in Pensions Bill' 25 October 2004; See also, HL Deb, 1 November 2004, c25-29

77 TPR, 'Regulator uses anti-avoidance powers on Sea Containers', (PN 07-10), 18 June 2007; Reasons of the determinations panel, June 2007; TPR, 'Regulator issues Financial Support Directions on Sea Containers', (PN 08/02, 6 February 2008); TPR, 'Reasons of the Determinations Panel of the Pensions Regulator in relation to the Determination Notices issued on 15 June 2007 re. The Sea Containers 1983 Pension Scheme and the Sea Containers 1990 Pension Scheme; NAO, 'The Pensions Regulator: Progress in establishing its new regulatory approach', HC 1035, 26 October 2007, p24

78 TPR Press Release, 'Regulator issues Financial Support Directions on Sea Containers' 6 Feb 2008

79 'Nortel-Lehman' Supreme Court judgement – regulator statement, 24 July 2013

80 'Pensions again – 'just when you thought it was safe to go into administration', Professor Ian Fletcher and Gary Squires, AlixPartners, Insolvency intelligence, 2014

In November 2016, TPR issued Warning Notices in respect of the BHS Pension Scheme – to Sir Philip Green, Taveta Investments Limited, Taveta Investments (No. 2) Limited, Dominic Chappell, Retail Acquisitions Limited., setting out evidence to support the use of its Contribution Notice and Financial Support Direction powers.[81] In February 2017, TPR it announced the terms of a settlement as a result of which enforcement action against Sir Philip Green, Taveta Investments Limited, Taveta Investments (No. 2) Limited would cease.[82]

In December 2016, TPR said it had secured a settlement with Coats for two of its schemes, covering approximately 90% of the total membership, following the issue of Warnings Notices.[83]

TPR's action against ITV in relation to the Box Clever Group Pension Scheme is an illustration of the time and effort it can take to get a result.[84] In January 2012, TPR explained its decision that Financial Support Directions should be issued in relation to the Box Clever Group Pension Scheme (one of them to ITV plc), on the basis that Box Clever Technology Ltd had been set up as part of a "highly leveraged transaction" and that the burden of servicing the resulting debt had been a major factor in its insolvency:

> […] the scheme's principal employer, Box Clever Technology Ltd ('BCT'), was set up by the Granada and Thorn groups as part of a highly leveraged transaction that effectively extracted value from the consumer rentals businesses of those groups, whilst leaving the possibility for Granada and Thorn to share in any future profit of BCT. A requirement of the transaction was that a pension scheme was set up for transferring employees. The ITV group received cash proceeds of approximately £500m as a result of the Box Clever transaction, which was paid from total debt of £860m raised by the BCT group. That borrowing was secured on all the assets of BCT and the other sponsoring employers of the scheme, but not the Granada or Thorn group companies, thereby insulating them from any downside. The burden of servicing this debt was a major factor in the insolvency of BCT group, including the sponsoring employers of the scheme, in 2003. The Panel did not find any misconduct on the part of the target companies, but considered FSDs to be an appropriate and reasonable response to these events.[85]

ITV referred the determination panel's decision to the Upper Tribunal, which heard the case in 2018 and decided that FSDs should be issued. ITV then appealed the Upper Tribunal's decision to the Court of Appeal. The Court of Appeal rejected the appeal (and upheld the Upper Tribunal's decision) in 2019.[86]

81 BHS: TPR launches enforcement action, November 2016
82 TPR, A quick guide to the BHS pension settlement, February 2017; TPR publishes report in BHS case, June 2017
83 TPR reaches £255m settlement in Coats anti-avoidance case, December 2016
84 Work and Pensions Committee, Defined Benefit Pension Schemes, December 2016
85 TPR Press Release, FSD determination in Box Clever case, 31 January 2012
86 Source: TPR

Proposals to strengthen the FSD regime

In its June 2018 consultation document, DWP proposed strengthening and improving the way FSDs worked by:

- Creating a single-stage process under which the Financial Support Direction would create a specific and enforceable obligation on the target (rather than this occurring at some later stage in the process);
- Tightening up the forms of financial support the target is required to make to the scheme, so that Financial Support Directions will either require a cash payment or impose a form of statutory guarantee in relation to some or all of the sponsoring employer's liabilities to the scheme;
- Allowing Financial Support Directions to be issued to a broader range of individuals, where they are associated with or connected to the sponsoring employer (provided other tests are met). This would mirror the scope of Contribution Notices;
- Amending the reasonableness test to make clear that the actions of a target in creating or increasing risk are a relevant (but not necessary) factor. This would mirror the scope of Contribution Notices;
- Providing TPR with a power to impose a Contribution Notice on any person associated or connected with the recipient of the Financial Support Direction;
- Exploring how and whether the 'lookback' period could be increased beyond two years;
- Providing the Regulator with a power to issue a Financial Support Direction after a scheme has entered the PPF and enable the PPF to enforce it in the form of a cash payment.[87]

In its response to consultation in September 2018, DWP said it would continue to work with TPR and the PPF to amend the FSD process to a single-stage process, in which the Determinations Panel imposes a particular form of amount of enforceable financial support on a target. It would change the name to Financial Support Notice (FSN).[88]

Proposals it had decided not to take forward were:

- Increasing the scope of FSD targets to include directors;
- Amending the reasonableness test to make clear that the actions of a target in creating or increasing risk would be a relevant factor;
- Enabling TPR to issue an FSD once a scheme has transferred to the PPF.

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87 DWP, Protecting Defined Benefit Pension Schemes – A Stronger Pensions Regulator, June 2018

88 DWP, Government Response to the Consultation on Protecting Defined Benefit Pension Schemes – A Stronger Pensions Regulator, Feb 2019

On the other hand, it would "pursue the proposal to broaden the targets of the FSD enforcement activity to ensure that pension obligations are met." [89]

2.3 Penalties

TPR currently has the power under section 10 of the *Pensions Act 1995* to issue a limited civil fine of up to £5,000 for individuals and £50,000 for corporate entities to penalise them for non-compliance with a wide range of duties.[90] It also has the ability to commence criminal proceedings in relation to failure to comply with certain duties under the *Pensions Act 2004:*

> […] including obstructing investigations under section 77 of the 2004 Pensions Act, and for providing it with false or misleading information under section 80 of the 2004 Pensions Act. The maximum sentence is an unlimited fine and, in some circumstances, imprisonment for a term not exceeding two years.[91]

In its December 2016 report on DB schemes, the Work and Pensions Select Committee recommended that the Government consult on giving TPR powers to impose punitive fines. It thought these fines could "treble the original demand" in a Contribution Notice or Financial Support Direction from TPR:

> 146. ***We recommend that in its forthcoming Green Paper the Government consult on giving TPR powers to add punitive fines to Contribution Notices and Financial Support Directions. These fines would have to be set at a high level to ensure they incentivised sponsors to properly fund pension schemes and seek clearance for corporate transactions which may be to a scheme's detriment. We recommend that fines that could treble the original demand be considered. The intention would be that such fines would not need to be imposed: they would act as a nuclear deterrent to avoidance.***[92]

In its Defined Benefit Pension Scheme Green Paper, the Government asked for views on whether the Pensions Regulator (TPR) "should be able to impose punitive fines for corporate transactions that are detrimental to schemes" and if so, in what circumstances.[93]

In its manifesto for the 2017 general election, the Conservative Party said it would give TPR "new powers to issue punitive fines for those found to have left a pension scheme under-resourced."[94]

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89 Ibid p30

90 The *Pensions Act 2008 ,* Part 1, chapter 2, enables penalties for failure to comply with employers' auto-enrolment duties.

91 TPR, Protecting Defined Benefit Pension Schemes – A Stronger Pensions Regulator, October 2018, p17

92 Work and Pensions Select Committee, Defined Benefit Pension Schemes, December 2016

93 DWP, Security and sustainability in Defined Benefit pension schemes, Cm 9412, February 2017, p73

94 Conservative Party, General Election Manifesto 2017

In *the Observer* on 21 January 2018, following the collapse of Carillion, the then Prime Minister, Theresa May said:

> In the spring, we will set out new tough new rules for executives who try to line their own pockets by putting their workers' pensions at risk – an unacceptable abuse that we will end.[95]

In the March 2018 White Paper, the Government said it would legislate to give TPR powers "to punish those who deliberately put their pension scheme at risk by introducing punitive fines."

> 14. We will legislate to introduce a proportionate and robust penalty regime to tackle irresponsible activities that may cause a material detriment to a pension scheme and may compromise the scheme's funding position.
>
> 15. This will strengthen the Regulator's existing anti-avoidance framework, and will give the Regulator an express power to penalise the targets of a contribution notice. This power will extend to individual company Directors.
>
> 16. The parameters of this new approach will be enacted in primary legislation.
>
> 17. To ensure members of Defined Benefit schemes are protected as far as possible and to deter activity that puts the security of members' benefits at risk, we will examine the feasibility of the penalty regime applying in respect of acts or omissions prior to enactment, in particular, after the date this document is published.
>
> 18. We will continue to work on the design of the new regime including the penalty levels, to ensure it remains proportionate and there are no unintended consequences. Although the details are still being developed, it is expected that the penalty will be linked to the contribution notice, effectively creating the possibility of a highly punitive fine being issued by the Regulator.
>
> 19. Through its operation of the regime over the last ten years, the Regulator has identified other ways in which its anti-avoidance powers could be enhanced. We will take this opportunity to review these powers more generally and, if needed, legislate to improve the Regulator's contribution notice and financial support directions powers, further strengthening the regime.[96]

It would also legislate to introduce a criminal offence to "punish those found to have committed wilful or grossly reckless behaviour in relation to a pension scheme and build on the existing process to support the disqualification of company directors."[97]

In December 2018, Dominic Chappell was ordered to pay more than £124,000 for failing to reveal information to TPR about the sale of BHS. The request had been made under section 72 of the *Pensions Act 2004* which enables TPR to require information and documents relevant to its statutory function. Failure to provide such information, without a

95 'Boardroom excesses can no longer be tolerated: the economy has to work for all', Theresa May, The Observer, 21 January 2018
96 DWP, Protecting Defined Benefit Pension Schemes, Cm 9591, March 2018
97 Ibid p6

reasonable excuse, is a criminal offence which can result in an unlimited fine.[98]

Consultation

The October 2018 consultation proposed a more comprehensive penalty regime, to cover both low-level compliance breaches and more serious offences. TPR and the courts would be able to consider the circumstances of the case and impose the most appropriate penalty, from a range of options, including:

> **Civil penalties (for low-level non-compliance)** – a fine up to £5,000 for an individual, and £50,000 in any other case, for any act or omission which contravenes any of the pension legislation to which section 10 of the Pensions Act 1995 applies;
>
> **Civil penalties (for more serious offences).** The Government proposed a new civil penalty (up to a maximum amount of £1 million) to provide TPR with the flexibility to issue different levels of fines for a range of further breaches (including non-compliance with new requirements to introduced following the White Paper).
>
> **Criminal sanctions** (which could include unlimited fines or custodial sentences) for the new criminal offences: wilful or grossly reckless behaviour in relation to a Defined Benefit pension scheme, non-compliance with a Contribution Notice and failure to comply with the Notifiable Events framework.[99]

In its response to consultation in February 2019, the Government said that the vast majority of respondents agreed that TPR needed additional resources to effectively enforce legal requirements.[100]

Pension Schemes Bill 2019/21

The table below lists the new civil and criminal offences to be introduced under the *Pension Schemes Bill [HL] 2019/21:*

98 TPR press release, 14 December 2018
99 DWP, Protecting Defined Benefit Pension Schemes – A Stronger Pensions Regulator, October 2018, p17-18
100 DWP, Protecting Defined Benefit Pension Schemes – A Stronger Pensions Regulator – Government response to consultation, February 2019, p24

New Offence	New Penalty	Target	Pension Schemes Bill 2019/20
Avoidance of employer debt; conduct risking accrued scheme benefits	Criminal offence: up to 7 years' imprisonment and/or a fine (unlimited, except in Scotland where limited to the statutory maximum); and/or new civil penalty up to a maximum of £1m	Any person	Clause 107 and 115
Failure to comply with a Contribution Notice	Criminal offence: fine (unlimited, except in Scotland, limited to the statutory maximum); and/or new civil penalty: up to a maximum of £1m	A person to whom a CN has been issued	Clause 106 and 115
Failure to comply with the Notifiable Events Framework	New civil penalty: up to a maximum of £1m	Sponsoring employers and trustees	Clause 108 and 115
Failure to comply with requirements for a Declaration of Intent	New civil penalty: up to a maximum of £1 m	Sponsoring employers and others associated or connected	Clause 109 and 115
Knowingly or recklessly providing false information to trustees	New civil penalty: up to a maximum of £1m	Any person who is required to provide information to trustees as prescribed	Clause 114
Non-compliance with information requests (including inspections and interviews) or delays in providing information	Fixed and escalating civil fine. The Government will develop the levels of fines as part of its secondary legislation package	Any person targeted by TPR under section 72-5 of Pensions Act (PA) 04	Clause 112
Knowingly or recklessly providing false information to TPR	New civil penalty: up to a maximum of £1m	Any person who is required to provide information to TPR as prescribed	Clause 113
Non-compliance with clearer funding standards	Strengthened section 231 (powers of TPR) scheme funding powers (such as improvement notices) of PA 2004	Trustees and sponsoring employers	Clause 123 and Schedule 10
Failure to provide a Chair's Statement, failure to provide on time or providing a poor quality statement	Existing civil penalty under section 10 of the PA 1995	Trustees and sponsoring employers	Clause 123 and Schedule 10

Debate

Scope of sanctions under clause 107

As stated above, clause 107 (sanctions for avoidance of employer debt) would amend the *Pensions Act 2004* to introduce new criminal offences and financial penalties for the avoidance of employer debt:

> 376. Subsection (2) of this clause creates two new offences including: section 58A: an offence for avoidance of employer debt and section 58B: an offence for conduct risking accrued scheme benefits.
>
> 377. Subsection (3) of this clause also creates two new civil penalties including: section 58C: a financial penalty for avoidance of employer debt and section 58D: a financial penalty for conduct risking accrued scheme benefits.[101]

At Committee Stage in the House of Lords, Peers questioned the circumstances in which these penalties would apply. Conservative Peer Baroness Neville Rolfe expressed concern that "the powers in clause 107 may be drawn too widely."[102] Former Labour Work and Pensions Secretary Lord Hutton of Furness expressed concerns, including:

- **Who can prosecute.** Whereas in the Green and White Papers, it had been clear that the Government had TPR in mind, "we now have the rather unsatisfactory state of affairs that not just the Pensions Regulator but the Secretary of State and the Director of Public Prosecutions can prosecute."
- **The scope of the new powers.** Whereas initially, the intention had been to catch the behaviour of "unscrupulous employers or directors of companies", it was now clear that it could "cover scheme trustees, actuaries and advisers, or pretty much anyone in a position to give advice on the management of a pension scheme."

101 Pension Schemes Bill 2019/21 – Explanatory Notes
102 HL Deb 24 February 2020 c53GC

- **Clarity over what was the appropriate penalty**. An offence under this section could be tried either on indictment or on summary conviction, suggesting it was "a serious and a less serious offence at the same time." This as "incomprehensible": it was a "serious offence that should be tried on indictment by an appropriate criminal prosecutor."[103]

Shadow Minister Baroness Sherlock said there was a need for "more clarity, for Parliament and the sector, as to how these provisions will operate in practice." For example, why had Ministers decided not to go with a test of "wilfully or recklessly" for deciding whether sanctions were appropriate and where it was setting the bar for material detriment.[104]

Responding, Earl Howe said examples of the types of acts being targeted were:

- The sale of an employer with a defined benefit scheme without replacing an existing parental guarantee over the employer's Section 75 debt, resulting in the loss of the guarantee, including failing to tell the trustees about the sale in advance;
- The purchase of a company, subsequent mismanagement of that company and extraction of value prior to it going into administration;
- The stripping of assets from the employer, resulting in a substantial weakening of support for the scheme.[105]

It was important for TPR to be able to respond appropriately where elements of the offences were met. The tests for an offence to have been committed included:

- whether a person had acted in a way, or engaged in a course of conduct, which "detrimentally affects in a material way the likelihood of accrued scheme benefits being received";
- whether they or ought to have known that the act or course of conduct would have this effect; and that
- the person did not have a "reasonable excuse."

The Government was consciously using the existing contribution notice tests as the basis for the new sanctions as they target similar behaviours and were already familiar to the industry.[106] The concept of materiality was included to indicate that consideration would need to be given to "the level of impact the conduct has on the likelihood of accrued scheme benefits."[107]

The inclusion of the Secretary of State as a potential prosecuting authority was to ensure that the "most serious conduct that harms pension schemes will remain punishable in the future" (for example, in the event of TPR ceasing to exist. It was not envisaged that the Secretary

[103] Ibid c54-6GC
[104] Ibid c59GC
[105] Ibid c60GC
[106] Ibid c61GC
[107] Ibid c62GC

of State will institute prosecutions where TPR or, where relevant, the Director of Public Prosecutions had decided against it.[108]

As regards the persons who could be subject to such a sanction, it was "the norm for criminal offences across the statutory book to be drafted as applying to any person." TPR would consult on guidance for the new offences, to be published prior to commencement.[109]

The issues were debated again at **Report Stage,** where Conservative Peers Baroness Altmann, Baroness Neville-Rolfe, Baroness Noakes and Lord Trenchard, expressed concern that as drafted the provisions could inject "great uncertainty into what is permitted behaviour by those involved in pensions administration" and to deter "ordinary pensions and business activity." Baroness Neville-Rolfe argued that it was wrong to extend criminal sanctions in "such a vague and general way." Lord Trenchard questioned the stated rationale for allowing the Secretary of State to prosecute (if TPR no longer existed, surely the whole system would need reform).[110]

Responding for the Government, Earl Howe said the aim was to "target individuals who intentionally or knowingly mishandle pension schemes or endanger workers' pensions by behaviours such as chronic mismanagement of a business or avoiding pension liabilities":

> The key point is the one that I made in Committee: that it is an offence only if the person intended to harm the scheme or should have known that the conduct would have that effect and they have no reasonable excuse for their actions. The decision on whether a person does or does not have a reasonable excuse and ultimately did or did not commit an offence in a particular case is a matter for the courts. However, in coming to such a verdict, the courts will have paid due regard to all the circumstances in the individual case in question. That, of course, includes coming to a view on whether the person's excuse for acting in that way was a reasonable one. The burden of proof on that question falls on the Pensions Regulator. In other words, the Pensions Regulator would need to prove that the actions of the individual were unreasonable.
>
> The other dimension of the issue is that it is important that, where the elements of an offence are met, no matter who has committed it, the regulator should be able to respond appropriately. Any restriction of the persons potentially in scope would create a loophole for those people to act in such a way.

TPR would publish guidance before the commencement of the provisions. The policy would be kept under review to ensure it met the Government's objectives.[111]

Baroness Noakes said she would reflect further and might return to the issue at Third Reading (now scheduled for 15 July).[112]

108 Ibid c63GC
109 Ibid c64GC
110 HL Deb 30 June 2020 c634-6
111 Ibid c637-8
112 Ibid c638

Fixed and escalating penalties

Liberal Democrat Peer, Lord Sharkey, questioned whether the maximum penalty to apply in some cases (£1 million) was high enough to influence behaviour given the resources of those on whom it might fall. The fact that the Bill included power to increase it by secondary legislation, suggested the Government might lack confidence in it.[113]

Baroness Stedman Scott responded that the Government had consulted on the proposals in its Green and White Papers:

> The £1 million maximum penalty was supported by the majority of respondents. The £1 million penalty is positioned as a mid-level sanction, between the lower £50,000 penalty for acts of non-compliance by corporates and £5,000 by individuals and the new higher-level criminal offences for serious wrongdoing that has an unlimited fine. The £1 million maximum level was also deemed to be appropriate as it is comparable with the average level of equivalent sanctions for financial crimes in the financial sector issued to individuals by the Financial Conduct Authority.[114]

The power to increase the maximum amount was needed to ensure that the penalty remained an effective deterrent. Devising penalties based on factors such as turnover, as some had proposed, would create uncertainty and the assumptions TPR would need to make would be open to challenge by the target.[115]

2.4 Restoration Orders

While the *Pensions Act 2004* was before Parliament (at Report Stage in the Commons) the Government introduced a further power, allowing TPR to impose a Restoration Order directing that the position of a scheme be "restored where the scheme has entered into a 'transaction at an undervalue' within a two-year period leading up to an insolvency event." Malcolm Wicks explained:

> A transaction at an undervalue is exactly what it says—a transaction involving scheme assets that results in the scheme receiving no consideration, or consideration that is less than the market value, in return. That could include, for example, trustees being persuaded to purchase a property on the basis of planning permission for a development that does not actually exist, or a director of a company persuading trustees to offer him a transfer on a very generous basis to prevent his benefits being reduced by the compensation cap should the scheme enter the PPF. There is currently provision in insolvency legislation retrospectively to undo "transactions at an undervalue" involving company assets, which occur in the run-up to insolvency. New clauses 12 to 16 introduce similar provision in respect of transactions involving scheme assets, in order both to protect scheme members from having the assets of their scheme unfairly depleted and to guard against the possibility of the PPF having to assume responsibility for such schemes where it otherwise would not have done so.[116]

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113 HL Deb 26 Feb 2020 c165v
114 Ibid c169GC
115 Ibid c170GC
116 HC Deb, 18 May 2004, c899-900

2.5 Regulated Apportionment Arrangements

Section 75 of the *Pensions Act 1995* provides that a debt is due from a sponsoring employer if they become insolvent or their scheme starts to wind up underfunded, or an application is made to the PPF for it to take responsibility for the scheme.[117]

The Labour Government made changes to the rules in the *Pensions Act 2004,* with the aim of improving protection for scheme members.[118] When these rules came into force in 2005, the rules included detailed provisions for dealing with the employer debt when an employer exited a multi-employer scheme:

- The employer debt was calculated on a 'full buy-out' basis,[119] but with provision for 'withdrawal arrangements' - allowing a lower amount to be paid on provision of a guarantee.
- The employer debt to be apportioned among the remaining employers.[120]

It made further changes to the rules in 2008 to provide more flexibility while at the same time aiming to prevent mis-use of the apportionment rule, with the aim of preventing a debt from being apportioned to weak employers or shell employers.[121] They also introduced the new option of Regulated Apportionment Arrangement (RAA), whereby debt could be apportioned outside the usual parameters, with the involvement of TPR. This could only take place where:

- A scheme was in a PPF assessment period, or one was likely to commence in future; and
- The PPF Board does not object (usually because it would result in a higher level of funding for the scheme than if the employer became insolvent).[122]

RAAs were intended to be extremely uncommon. In deciding whether to allow one, TPR considers relevant circumstances, which may include:

> - whether insolvency of the employer would be otherwise inevitable or whether there could be other solutions (including funding options for the scheme) which would avoid insolvency;
> - whether the scheme might receive more from an insolvency;
> - whether a better outcome might otherwise be attained for the scheme by other means (including through the use of the regulator's powers where relevant);
> - the position of the rest of the employer group; and

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117 As amended by *Pensions Act 2004,* s271; explanatory notes, para 1065; *Occupational Pension Schemes (Employer Debt) Regulations 2005 (SI 2005/678)*
118 HL Deb 13 October 2004 s83-4; *Pensions Act 2004 s270*
119 The amount that would need to be paid to secure buy out of the pension's full liabilities with an insurance company
120 Explanatory Memorandum to SI 2008/731
121 Ibid para 7.4-8
122 Explanatory Memorandum to SI 2008/731

- the outcome of the proposals for other creditors.[123]

In an August 2016 paper setting out its Approach to Employer Restructuring, the PPF explained that its aim was to "make sure that the pension scheme is in a much better position than it would have been if we had done nothing."

Some examples in practice…

TPR approved an RAA in relation to the BMI Pension Scheme, allowing for its controlled entry into the PPF. An earlier proposal, which would have involved keeping the scheme open was rejected by TPR. This was because the proposed voluntary contributions from Lufthansa (which had no statutory obligation to fund the scheme) were insufficient in isolation to prevent a deterioration in the Scheme's funding position, leaving the proposal almost wholly reliant on investment outperformance. TPR considered that this posed unacceptable risks to members' benefits and PPF levy payers and therefore worked to explore alternatives:

> Following further discussions, the regulator issued a clearance statement for a second proposal which involved a controlled entry to the PPF via a rarely used mechanism called a Regulated Apportionment Arrangement (RAA). Under the arrangement, the Scheme (and therefore PPF) received £16 million, significantly more than would have been received from the insolvency of British Midland Airways Limited (BMAL), the Scheme's statutory employer. In addition, Lufthansa provided a further voluntary contribution of £84 million to top up members' benefits outside the PPF.[124]

An RAA was also approved in the case of the Kodak Pension Plan. Members were given the option to transfer to a new scheme that would offer lower benefits than they had accrued but better benefits than PPF compensation levels, or members could remain the existing scheme which would transfer to the PPF:

> In January 2012, the Kodak group's US parent, Eastman Kodak Company, entered Chapter 11 bankruptcy proceedings. This meant that the Kodak Pension Plan was at risk of losing both existing support from the wider Kodak group and ongoing contributions from its sponsoring employer.
>
> In order to maximise the value available to the Kodak Pension Plan, a deal was agreed under which the trustees acquired Kodak's cash generative 'personalised imaging' and 'document imaging' businesses. In exchange, the Kodak group was released from its liabilities to the Kodak Pension Plan.
>
> Despite the acquisition, there remained serious doubts as to whether the assets could provide adequate support for the scheme's existing liabilities. Therefore members were given the option to transfer to a new scheme which would offer benefits better than the Pension Protection Fund, but lower than in the Kodak Pension Plan. Members representing in excess of 94% of liabilities have decided to transfer.

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[123] TPR, RAAs and employer insolvency, August 2010

[124] Regulator publishes report on BMI pension scheme, PN12-15, 31 May 2012

> The regulator and the trustees have agreed a governance framework to limit risks to member benefits and the PPF, including monitoring the performance of the acquired businesses and imposing restrictions on discretionary pension benefit awards and investments.[125]

The Halcrow Pension Scheme was in deficit and its sponsoring employers were unable to afford the necessary contributions to repair it. In this case, TPR, the PPF, the employers (Halcrow Group Limited and its parent company CH2M HILL) and the pension scheme trustees negotiated a proposal that would involve offering members the chance to transfer to a new scheme or remain in the existing one and transfer to the PPF. CH2M HILL would make a cash payment to the original scheme (the Halcrow Pension Scheme), together with an equity stake in HGL in view of the loss of employer support through an RAA.[126]

In May 2017, TPR announced that it had reached agreement in principle on the key commercial terms of an RAA in relation to the British Steel Pension Scheme.[127]

In June 2017, TPR announced an RAA in relation to the Hoover Pension Scheme, which would "receive £60 million from Hoover and is expected to transfer into the Pension Protection Fund (PPF). "[128]

In September 2017, TPR granted formal approval to a proposal from Tata Steel UK Ltd to separate itself from the British Steel Pension Scheme (BSPS), through an RAA. The BSPS would receive £550 million from the Tata Steel Group and a 33% equity stake in Tata Steel UK Ltd. Scheme members would be given the opportunity to transfer to a new BSPS (which would provide indexation that was less generous than the current scheme but higher than the PPF).[129] This is discussed in more detail in Library Briefing Paper CBP-05656 Occupational pension increases (September 2017) (section 3).

Proposals for reform

The Work and Pensions Select Committee said it thought TPR should become involved at an earlier stage and take a more iterative approach:

> **92. The Regulated Apportionment Arrangement (RAA) is a means of negotiating an outcome for scheme members that is better than the PPF in instances where a sponsoring employer is in mortal danger. When agreed, it can produce results that are better for pensioners, better for employers and better for the PPF than insolvency. It is, however, very rarely used, and the process includes potentially harmful**

[125] 'Kodak and UK Coal case reports published,' TPR press release, Monday 3 November 2014; Report in relation to the Kodak Pension Plan (November 2014)

[126] TPR, Regulatory Intervention Report issued under s89 of the Pensions Act 2004 in relation to Halcrow Pension Scheme, July 2016

[127] TPR Statement on British Steel Pension Scheme, PN 17/25, 17 May 2017; For more detail, see Library Briefing Paper SN-05656 Occupational pension increases (June 2017), section 3.

[128] TPR finalises pensions deal with Hoover, 2 June 2017

[129] TPR, Tata Steel UK's proposal to restructure the British Steel Pension Scheme agreed by TPR, PN 17-48, 11 August 2017; BSPS Trustees, British Steel Pension Scheme Separated from Tata Steel UK Limited, 11 September 2017

delays. It is an emergency measure, but it does not operate at an emergency pace.

93.We recommend that in its forthcoming Green Paper the Government consult on:

- **reducing the interval, currently 28 days, between TPR issuing a warning notice of an impending RAA and issuing a final notice; and**
- **relaxing the requirement for insolvency to be inevitable within 12 months for an RAA to be approved.**

We further recommend that TPR guidance be amended to encourage its involvement at an earlier stage in the formulation of RAA proposals in order to facilitate a more iterative approach.[130]

In its February 2017 DB Green Paper, the Government asked for views on proposals to allow struggling businesses to separate from scheme sponsors more easily, including by widening the criteria for RAAs. It commented that:

> 227. Our analysis highlights that there appears to be a group of employers who are likely but not certain to become insolvent before the completion of the recovery plan or members benefits are paid in full. However, many of these employers may not be able to access an RAA as it is not clear that they will become insolvent in the next 12 months. For the schemes sponsored by these employers, the current system does not offer any alternative. Their only option is to aim for investment returns to enable them to reach full funding or for the business to improve and generate more cash. But the burden of the pension scheme may itself be compromising the ability of the business to invest and recover, or to restructure. This also creates a risk for PPF members and levy payers because there is a risk that the PPF deficit could grow very substantially in the run up to a likely future insolvency.[131]

It said there could be a considerable prize – giving struggling employers the chance to emerge as a sustainable business and generate more value for the pension scheme – but that it would also require a "different trade-off" between sponsors, members and the PPF levy payers and would raise moral hazard issues:

> 229. It is also important to recognise that the options that involve a 'transfer of wealth' from the members to the sponsor would raise moral hazard issues and there would need to be appropriate quid pro quo provisions in place. For example similar provisions to the condition for RAAs where the scheme would need to receive more than it would otherwise on insolvency, to ensure that the scheme is being treated fairly compared to other creditors to the employer.[132]

Respondents to the Green Paper recognised the tensions. The TUC said trade unions should be involved in the consultation but that there was a case for considering whether "a special measures process could be put

130 Work and Pensions Select Committee, Defined benefit pension schemes, December 2016
131 Cm 9412, Feb 2017
132 Ibid

in place at an earlier stage than available under the current regime as a means of securing a better deal than would be available at the point of insolvency."[133] The PPF thought the requirement that insolvency must be inevitable in the next 12 months was overly restrictive and might limit the restructuring action that can take place whilst value remains in the employer. However, any amendments would need to retain strong safeguards to protect against "pension dumping", including ensuring that the outcome was better for the scheme than the alternative and that the employer would otherwise be expected to become insolvent.[134] The PLSA said it "should be easier to separate schemes from struggling employers."[135] The Association of Consulting Actuaries said the test for allowing an RAA should be based on the members' best interests rather than explicitly requiring insolvency in the near future.[136]

In the White Paper, the Government said it would look further at whether changes could be made to the RAA process without increasing the risks to scheme members:

> 207. We discussed the idea of making changes to the RAA process in the Green Paper. Around half of the respondents suggested that the current process is too complex, and that this complexity can prevent employers from making use of an RAA even where it would be in both the employer and the scheme's interest. They argued that making the process simpler could enable more businesses who would otherwise fail due to loss of investment or restructuring to benefit from RAAs, leading to better outcomes for current and future employees.
>
> 208. However, the other half of respondents were opposed the idea of any changes to the RAA process. Respondents argued that making it easier for employers to go through an RAA increased the risk that unscrupulous employers could seek to manipulate their circumstances in order to be able to separate themselves from their scheme.
>
> 209. We have given careful thought to whether, and how, we should make any changes to simplify the RAA process. We believe that an RAA can be helpful for both employers and schemes in some circumstances. We want to ensure that RAAs can be accessed by the right employers at the right time where an objective assessment suggests that they are at risk of insolvency and are not likely to be able to continue to support their Defined Benefit scheme.
>
> 210. However, we recognise that there is a risk in allowing more employers to go through an RAA process. It is important that we do not increase the risk to members by making changes.
>
> 211. We are therefore committing to working closely with the Regulator, PPF, stakeholders and the pensions industry to look at whether it is possible, without increasing risk to scheme members, to make improvements to the RAA process, thereby increasing the potential for positive outcomes for businesses which might otherwise fail.[137]

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133 TUC, Response to Green Paper, May 2017
134 PPF Response to Green Paper, May 2017
135 PLSA, Response to Green Paper, May 2017
136 ACA, Response to Green Paper, May 2017
137 DWP, Protecting Defined Benefit Pension Schemes, Cm 9591, March 2018

2.6 Clearance statements

The clearance procedure was introduced to enable companies undergoing restructuring to gain assurance that TPR's anti-avoidance powers would not be used in relation to the transaction. The guidance states:

> 'Clearance' is the term used to describe the voluntary process of obtaining a clearance statement from the regulator. A clearance statement gives assurance that, based on the information provided, the regulator will not use its anti-avoidance powers to issue to the applicants either contribution notices or financial support directions in relation to a defined benefit occupational pension scheme and a particular event. 'Events' include transactions, agreements, decisions, other acts and failures to act.[138]

TPR seeks to balance different factors in reaching a decision:

- The regulator's preferred outcome is an appropriately funded scheme with a solvent employer.
- The regulator will deploy its resources in a risk-based manner, targeting risk in a proportionate, responsive, flexible, pragmatic, consistent, transparent and reasonable way.
- The regulator will seek to protect members' benefits and reduce the risk of calls on the PPF, while at the same time recognising commercial activity and business needs.[139]

It can issue an assurance that its CN and FSD powers will not be used after the event. It strongly advises seeking clearance where "there is an event that may be materially detrimental to the ability of the scheme to meet pensions liabilities – such as a change of ownership."[140] It can not stop corporate transactions from proceeding, only decline to issue a clearance statement.

TPR published guidance on clearance in March 2010.

The Green Paper

The Work and Pensions Select Committee noted that clearance applications had declined substantially, falling from 263 in 2005-06 to nine in 2015-16. It recommended that the Government consult on new rules for situations where clearance was mandatory:

> **140. Clearance has the clear benefit of enabling TPR to tackle potential moral hazard implications of corporate transactions head-on rather than after the event, while providing comfort and certainty to the scheme members and sponsoring firm. Clearance is far preferable to the drawn-out—and resource-intensive—legal process of enforcement action. It is, however, voluntary and employers are increasingly skipping it: there were 263 applications in 2005–06 but just nine in 2015–16. The incentives to seek clearance are currently weak. Some**

138 TPR, Clearance Guidance, March 2010 - introduction
139 TPR, Clearance Guidance, March 2010; Earlier version dated March 2008,
140 Article by Tony Hobman, Chief Executive of the Pensions Regulator in HR Director, issue 38, June 2007

> **unscrupulous sponsors may well be calculating that they are better off risking a protracted anti-avoidance battle than coming to an immediate pension settlement.**
>
> 141. We recommend that in its forthcoming Green Paper the Government consult on proposals to require advance clearance from TPR for certain corporate transactions that could be materially detrimental to the funding position of a DB scheme. The circumstances in which clearance was compulsory would have to be narrow to prevent a disproportionate effect on normal economic activity. They might include the sale or merger of a scheme sponsor where the pension deficit is higher than a fixed proportion of the value of the company. It is also reasonable to expect any prospective purchaser to have a credible plan for tackling a substantial pension deficit.[141]

In its DB Green Paper, DWP said "very significant difficulties" would need to be overcome before clearance could be required in certain specified circumstances:

> 314. Making clearance a compulsory procedure even in very limited circumstances has the potential to make turnarounds more difficult and lead to more businesses being placed into insolvency. With turnarounds, there is often limited time available in which to conclude a deal. Businesses with an attached DB scheme could find themselves as unattractive investment targets. That could put more schemes into the PPF with consequences for the members and the PPF itself.
>
> 315. Giving the Regulator this power could also reduce the attractiveness of UK companies with DB pension schemes to investors, especially if investors believe this could restrict the ability of these companies to speedily restructure their operations should they fall into difficulty in the future.
>
> 316. The current regime seeks to balance the tension between the aim of protecting the pension scheme and the future prospects of the employees who also have an interest in the outcome of any deal. Any revised regime would also need to manage this difficult balance as it is inevitable that there will be circumstances where the business restructuring should proceed to ensure that jobs are saved even when the risks to the scheme have not been fully mitigated.
>
> 317. Some stakeholders have also pointed out that there are business decisions which are less recognisable as corporate transactions, but are likely to affect the ability of the sponsor to fund their DB scheme. For example, moving assets from the sponsor to another part of the corporate group cannot be effectively managed/controlled through a prospective clearance regime, and can only be addressed retrospectively. [142]

It said that another, less stringent approach – which could encourage employers to engage with TPR earlier - would be to give it power to levy a significant fine (in addition to pursuing the employer for any support) where activity was shown to be detrimental without appropriate mitigation. Criteria would need to be very clear to prevent TPR being

[141] Ibid
[142] DWP, Security and Sustainability in Defined Benefit Pension Schemes, Cm 9412, Feb 2017, p 7

overwhelmed with clearance applications and corporate activity being held up.[143]

The Government asked for views on whether it would be possible to "design a system of compulsory proactive clearance by the Regulator of certain corporate transactions without significant detriment to legitimate business activity."[144]

In response, TPR said it did not think mandatory clearance would be a proportionate approach. Instead it advocated strengthening the position of trustees and incentivising employers to submit clearance applications, perhaps by enabling the imposition of substantive fines where employers are found to have avoided pension liabilities.[145] The trade union, Prospect, agreed, arguing that the focus should be on ensuring that trustees and trade unions have "access to sufficient corporate information to enable an informed decision to be made on whether such any transaction should be approved or not."[146]

The White Paper

In its March 2018 White Paper, the Government said most respondents to the Green Paper were concerned that proposals for targeted mandatory clearance could "stifle legitimate business activity such as corporate restructuring and could adversely impact on employment prospects." The Government would:

> […] strengthen the clearance regime so that sponsoring employers give sufficient regard to their pension scheme during corporate transactions, by building on existing processes and considering what new measures might be necessary. We will continue to work with the Regulator, industry and other relevant parties to understand how any new proposals might be introduced without inhibiting legitimate business activities.[147]

Response to consultation

In February 2019, the Government said that TPR would review its guidance on the clearance process to clarify its expectations as to what employers and trustees should do in relation to:

- The Material Detriment definition and how applicants and trustees should approach the test;
- Revision of the definition of event types, including the circumstances in which clearance is given in relation to Financial Support Directions;
- More information about how the clearance process works.[148]

143 Ibid, para 320
144 Ibid, p 73
145 TPR Green Paper response, May 2017
146 Prospect Green Paper response, May 2017)
147 DWP, Protecting Defined Benefit Pension Schemes- A Stronger Pensions Regulator, Cm 9591, December 2018
148 DWP, Protecting Defined Benefit Pension Schemes – A Stronger Pensions Regulator, February 2019, p15

2.7 The notifiable events framework

The notifiable events framework is designed to give TPR early warning of a possible call on the Pension Protection Fund. Schemes that are eligible for the PPF, and their employer, are required to notify TPR of certain types of event. Notifiable events are those which have the potential to cause harm to a pension scheme – for example, by increasing the chance of the sponsoring employer becoming insolvent or by impacting on the employer covenant.[149]

The February 2017 Green Paper acknowledged some concern that this was not working as well as it should:

> 310. Duties to notify the Regulator of certain corporate transactions already exist within pension legislation. The duty falls on the trustees and employer through the notifiable events framework, with penalties for non-compliance. However, notification often occurs very close to the completion of the transaction, and trustees are sometimes not informed at all, which means that the Regulator is unable to act to prevent the transaction. There is some concern, shared by the Regulator, that the current regime is not working as well as it could.[150]

The March 2018 White Paper proposed areas for improvement, in particular:

> - coverage of the notifiable events framework – we will review whether it covers all relevant transactions and widen these to include anything that is currently missing; and
> - timing of the notifiable events framework – the framework currently requires businesses to inform the Regulator as soon as reasonably practical but without further definition. In practice, in some cases, this has meant not until (or after) the events actually occur. We think that this timing needs clarifying so that the Regulator is made aware at an earlier stage in consideration and can engage in discussions sooner.[151]

The June 2018 consultation document proposed changes intended to ensure that TPR was better sighted on business transactions and events which might have a detrimental impact on a pension scheme. Proposed additions to the list of 'notifiable events' included:

- Sale of a material part of a sponsoring employer's business or assets of a scheme employer which has funding responsibility for at least 20% of the scheme's liabilities;
- Granting of security on a debt to give it priority over debt the scheme;
- Significant restructuring of the employer's board of directors and certain senior management appointments;

[149] *Pensions Act 2004*, s69; SI 2005/900; TPR Code of Practice 2: the notifiable events framework; TPR guidance, Notifiable events framework
[150] Cm 9412, Feb 2017, para 69 and 310
[151] DWP, Protecting Defined Benefit Pension Schemes, Cm 9591, March 2018, para 37

- Sponsoring employer taking independent pre-appointment insolvency/restructuring advice (such as an independent business review).

The breach of banking covenant notifiable event would be extended to include 'covenant deferral, amendment or waiver' (i.e; a wider set of circumstances).

Some commentators had called for dividend payments to be considered. However, the Department for Business, Energy and Industrial Strategy was looking at this as part of its consultation on corporate governance.

In order be proportionate, only transactions exceeding a certain risk threshold should be notifiable, for example, where the scheme is underfunded on a pre-determined basis. In its response to consultation in February 2019, the Government said it would introduce the following new employer-related notifiable events:

- Sale of a material proportion of the business or assets of a scheme employer which has funding responsibility for at least 20% of the scheme's liabilities; and
- Granting of security on a debt to give it priority over debt to the scheme.[152]

Declarations of intent

The White Paper said that for some notifiable event transactions, the employer would need to issue a 'Declaration of Intent' setting out the implications of the transaction for the scheme and how this would be mitigated. This would:

> oblige corporations to think about the effect of corporate decisions on affected pension schemes in more detail and at an appropriately early point in the transaction process. Declarations of Intent will therefore form part of an enhanced early warning system as all parties will be aware of concerns and proposed mitigations earlier than is currently the case, and will have a clear record of all agreements reached.

The transactions this would apply to were:

- Sale of controlling interest in a scheme employer;
- Sale of the business or assets of a scheme employer; and
- Granting of security in priority to scheme debt.[153]

There are provisions in clauses 108-12 of the *Pension Schemes Bill 2019/21* to give TPR "a more coherent set of information gathering powers."[154]

2.8 Trustees

The vast majority of private sector DB schemes are set up under trust.[155] This means that they are legally separate from the sponsoring employer

152 Government Response to the Consultation on Protecting Defined Benefit Pension Schemes – A Stronger Pensions Regulator, February 2019, p8-9
153 Ibid, p13-14
154 *Pension Schemes Bill [HL] 2019 –* Explanatory Notes, para 23 and pp46-50
155 Ibid. The exception is statutory schemes – usually public sector

and trustees are responsible for running the scheme – including investment choices and agreeing with the employer assumptions to be used in scheme valuations and recovery plans where a scheme is in deficit. The February 2017 DB Green Paper describes them as "very much the 'first line of defence' for scheme members."[156]

TPR provides guidance and support to trustees to help them understand their duties and had "a range of powers to intervene" where it has "concerns about a funding plan or where an employer is seeking to walk away from its pension promises."[157]

It also has power to appoint independent trustees where it is satisfied that this is reasonable to do so in order:

- to secure that the trustees as a whole have, or exercise the necessary knowledge and skill for the proper administration of the scheme;
- to secure that the number of trustees is sufficient for the proper administration of the scheme;
- to secure the proper use or application of the scheme's assets, or
- otherwise to protect the interests of the generality of members of the scheme.[158]

Between 2010 and May 2015, TPR appointed an independent trustee in respect of 184 appointments.[159] For example, in 2007, it used these powers in relation to the Telent Pension Scheme, due to concerns about potential conflicts of interest.[160]

In its December 2016 report, the Work and Pensions Committee recommended that the Government consult on "proposals to give trustees powers to demand timely information from sponsors." This was to prevent trustees being "kept in the dark about information crucial to them carrying out their duties effectively."[161]

The February 2017 Green Paper asked:

- Should trustees be given extra powers such as powers to demand timely information from sponsors, to strengthen their position? If so, what extra powers might be helpful?

Should trustees be consulted when the employer plans to pay dividends if the scheme is underfunded – and if so, what level of funding?[162]

156 Ibid, p15
157 Ibid
158 Section 7, Pensions Act 1995
159 TPR FOI response, May 2015
160 TPR Press Release, PN07-18, 'Regulator confirms use of powers on Telent pension scheme', 9 November 2007; TPR Press Release, PN 08-08, 11 April 2008, Telent pension scheme undertaking received,
161 Defined Benefit pension schemes, Work and Pensions Committee, December 2016, para 13
162 DWP, Security and Sustainability in Defined Benefit Pension Schemes, Cm 9410, December 2016, p73

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