

Response ID ANON-SC19-FURR-Y

Submitted to **Protecting Defined Benefit Pension Schemes - A Stronger Pensions Regulator**

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About you

1 What is your name?

What is your name?:

David Robertson

2 Are you answering on behalf of:

An organisation (in an official capacity)

If you are answering on behalf of a pension scheme, an organisation or other, please state the name :

Employer Covenant Working Group (ECWG)

3 Which of the following best describes you?

Representative body

If "Other" please specify:

4 Trustees - Which of the following best describes you?

Not Applicable

5 Employers - Which of the following best describes your organisation?

Not Applicable

6 Pension Professionals - Which option best describes your profession?

Other

If "Other" please specify :

Professionals dealing with covenant advisory work

7 Representative bodies - Who are you responding on behalf of?

Please specify :

Employer Covenant Working Group

Ministerial Foreword

Introduction

Introduction - A Stronger Pensions Regulator

The Consultation Process

Corporate Transaction Oversight - Notifiable Events Framework - Introduction

Corporate Transaction Oversight - Notifiable Events Framework - Our Proposals

Corporate Transaction Oversight - Notifiable Events Framework - Our Proposals (Continuation)

Corporate Transaction Oversight - Notifiable Events Framework - Questions

8 We have set out a number of proposed changes to the existing notifiable events framework. Do these proposals strike the right balance between improved regulations on business and protecting pensions?

Please provide your comments in the box below:

We agree with your proposal re wrongful trading.

We question why the proposed notifiable event triggered by sale of a material proportion of business or assets should be qualified by a specific percentage of

scheme liabilities. For example, this would preclude notification of the removal from the legal covenant structure of a 'last man standing' employer with a relatively large assets or profit generation if only a small amount of liabilities is able to be attributed to it.

The proposal to include additional objective notifiable events, that are likely to indicate distress or significant change i.e. in relation to banking covenants and board composition, appear both sensible and practical.

The proposal to include the taking of pre-insolvency or restructuring advice as notifiable is also sensible in principle, although there is a concern that this could deter management from taking such advice and this is open to subjectivity or ambiguity about when or what to notify. For example, whether an 'independent business review' will be commissioned by one or more lending banks will depend very much on the context of the case. What is less open to such subjectivity is the identity of the party or parties who commission the engagement, or to whom the reviewer has a duty of care. In a distress scenario, the lending bank or other creditor(s) are likely to be involved. One option therefore might be for this proposal to be widened to include any review or advice either commissioned by, or with a duty to, a third party with the employer's involvement.

In relation to the subjective, transaction-type events, experience shows that the impact of any corporate transaction or event on the covenant of a sponsoring employer will be highly specific to the circumstances of the transaction taking account of a range of issues "in-the-round". Experience also shows that ostensibly similar transactions can take many forms dependent upon the objectives of the parties, tax planning, corporate structure etc. For these reasons, there is a significant danger that any attempt to be prescriptive on the types of transaction that should be caught within an enhanced notifiable events framework would be as likely to miss relevant transactions as it would be to catch non-relevant transactions.

Such transactions are of concern if they (i) reduce the ability of the sponsoring employer to put cash into the scheme as and when required, and/or (ii) Increase the likelihood of a default event occurring (e.g. as a result of tighter lending covenants), and/or (iii) reduce the funds available to the scheme in the event of a default occurring.

The Employer Covenant Working Group ("ECWG") published a guide for practitioners in December 2016 ("Transactions in a non-distressed environment"), in which such transactions were summarised as follows:

- (1) Transactions involving a change in share or asset ownership (e.g. mergers & acquisitions, demergers, disposals of business, disposal of assets, creation or termination of joint ventures);
- (2) Internal reorganisations (e.g. corporate entity streamlining, divisional activity realignment, shared service arrangements);
- (3) Refinancings (e.g. refinancing of existing debt or changes to capital structure – including the granting of new or additional senior-ranking security);
- (4) Value distributions (e.g. dividends, share buy-backs and other distributions and transfers of value within and outwith the group).

We consider it good market practice to expect any sponsoring employer to advise the Trustee of any such transaction and to expect the Trustee to review each transaction to consider its impact on covenant strength and to ensure the fair treatment in the use of any proceeds arising from such transactions. The Trustee should take a risk-based and proportionate approach to such reviews, taking account of all issues 'in the round'.

We therefore think that a proposal to include all four such types of such transaction within the notifiable event framework would serve to capture all relevant transactions and not place any additional burden on employers and/or schemes that already adopt a proper approach to employer covenant.

9 Alternatively, are there any other significant business events which you think should be captured?

Please provide your comments in the box below:

10 Have we captured the right criteria for a significant change in the make-up of a board of directors?

Please provide your comments in the box below:

This appears sensible. We would propose that a further event would be the addition of new statutory directors whose number would account for a majority of the board e.g. if a board has three directors, the addition of a further four new directors (who could outvote the incumbent board) would be a notifiable event.

11 We are proposing to bring forward or specify more clearly the timing of reporting notification of certain events, for instance to the point at which Heads of Terms are agreed for some transactions. Is this appropriate or is there a better time/ event to pin the reporting notification to?

Please provide your comments in the box below:

This appears appropriate. However, in practice the timing of the notification to the Regulator has been less of an issue than the Regulator's unwillingness to engage, sometime until after a transaction has completed. Transactions differ widely in their structure and timing - in many cases there is no 'Heads of Terms' stage for instance and the regulatory steer should be towards notification at an early stage, for example when the board has given in principle approval to proceed with the deal. A significant improvement would be for the Regulator to engage with all parties in advance of completion where the Trustee has asked it to do so. This is an area where case studies and tPR guidance would be useful.

For the avoidance of doubt, an employer should also notify the Trustee of any employer notifiable event.

We note that boards and management teams of UK listed companies and those subject to the UK Takeover Code may have concerns about their legal exposure if notifications (and declarations of intent) have to be made to the pension trustees; this may be, for instance about the sharing of potentially price sensitive information or making with a large number of people 'insiders'. These concerns could hamper the notifiable events and declaration of declaration of intent framework working in a clear and straightforward way. We suggest therefore that there be liaison with the UK Listing Authority and Takeover Panel in this regard.

12 What is the likely impact (either direct or indirect) on business of sponsoring employers being required to report earlier?

Please provide your comments in the box below:

We anticipate little, if any, impact on sponsoring employers who already take proper account of their responsibilities towards the schemes, on the basis that the Regulator accepts outcomes agreed between the employer and the Trustee that lie within a realistic corridor of professional judgement. The process could however become bogged down if the Regulator adopts an overly prescriptive or "tick box" approach to such transactions. To ensure the smooth running of such a comprehensive notification framework, we would note the need for appropriate resources by tPR, including for example the use of a panel system, staffed with experienced practitioners, who could be called upon to review agreed transactions (perhaps on a sample basis) and to report and make recommendations on more involved or contentious transactions.

13 How could the framework be modified to ensure that any adverse impact is mitigated?

Please provide your comments in the box below:

14 Are there any additional changes that could further improve the design of the framework for sponsoring employers, trustees and the Regulator?

Please provide your comments in the box below:

We would suggest the promotion of a comprehensive proactive communication programme to accompany any changes to legislation, with the objective of encouraging an environment of co-operation and shared purpose between sponsoring employers and Trustees, to guard against a "beat the system" or combative environment arising.

Corporate Transaction Oversight - Declaration Of Intent - Our Proposals

Corporate Transaction Oversight - Declaration Of Intent - Questions

15 We have set out a number of proposed transactions which would trigger a Declaration of Intent. Do these proposals strike the right balance between improved regulations on business and protecting pensions?

Please provide your comments in the box below:

In relation to subjective, transaction-type events, experience shows that the impact of any corporate transaction or event on the covenant of a sponsoring employer will be highly specific to the circumstances of the transaction taking account of a range of issues 'in-the-round'.

The declaration of intent should relate to any transaction which may be materially detrimental to the covenant.

It should be clear what form the Declaration should take and how extensive it should be.

Given that the Declaration is proposed to relate to transactions of highest potential risk, we note that the Trustees will already have statements relating to IRM, as well as the SIP and SFP.

We understand the proposal to be that the Declaration is issued to tPR and trustees under confidentiality.

In order to deal with the complexity of other transactions, it would be useful if the Trustee could be given the power to request the Employer to produce a Declaration of Intent in all other circumstances where, with the benefit of transaction knowledge and in the context of the relevant pension obligations of the employer [or ex-employer], it considers the transaction to be within a "high potential risk" category. Such a request should be shared with the Regulator.

16 Alternatively, are there any other significant business transactions which you think should be captured?

Please provide your comments in the box below:

17 Is there any further information which could be included in a Declaration of Intent to improve understanding of the proposals to strengthen the position of the pension scheme?

Please provide your comments in the box below:

The information contained within the Declaration should be set within the context of the pension obligations for the sponsoring employer, and its group where relevant.

18 At which point in the transaction process should sponsoring employers a) engage with trustees and b) issue a Declaration of Intent to them?

Please provide your comments in the box below:

These both should be as early as possible and certainly in advance of Heads of Terms (if any) being agreed. There is a practical balance to be struck between giving parties sufficient time to intercede and not hindering transactions. Given the considerable variety of transaction types and timings, it might be helpful for this to be referenced to what is reasonable in the circumstances, with the regulatory guidance to give examples. This is likely to require at least a number of days before the terms of the transaction have been agreed.

19 What would be the impact (both direct and indirect) of our proposals on businesses, for example on transactions or administration costs of notification?

Please provide your comments in the box below:

We are not in a position to assess the impact, but would anticipate that such costs should typically be a de minimis proportion of the cost of many transactions for

sponsoring employers who already take proper account of their responsibilities towards their schemes. This is on the basis that the Pensions Regulator accepts outcomes agreed between the employer and the Trustee that lie within a realistic corridor of professional judgement. This would encourage (force) employers and trustees to take proper advice in relation to such transaction – which already happens in well-run employers and schemes.

There may be the risk of substantial additional legal fees being incurred, at least in the early stages of adoption, while employers and trustees agree terms. This could be mitigated by the Regulator by the sharing of guidance, case studies and best practice wording.

20 What more could we do to increase trustees' involvement in negotiations to ensure there is due consideration of the potential transactional risks to pension schemes?

Please provide your comments in the box below:

The process could become bogged down if the Regulator adopts an overly prescriptive or 'tick box' approach to such transactions.

It might be helpful for the Declaration of Intent process to make provision for information sharing with the Trustees and their advisers, meetings and formal written responses to Trustee enquiries.

To ensure the smooth running of such a comprehensive notification framework, we would note the need for sufficient resources supplemented for example by a panel system, staffed with experienced practitioners, who could be called upon to review agreed transactions (perhaps on a sample basis) and to adjudicate on more involved or contentious transactions. Such an ease of Regulator engagement approach would encourage parties to negotiate early and fairly. This, combined with a more punitive system to deal with rogue elements would serve to increase trustee involvement at an early stage.

Corporate Transaction Oversight - Voluntary Clearance - Our Proposals

Corporate Transaction Oversight - Voluntary Clearance - Questions

21 Are these the right areas for the Pensions Regulator to focus on in relation to improvements to their existing guidance?

Please provide your comments in the box below:

The Clearance regime is currently an employer-led process: if it does not consider a proposed transaction to be materially detrimental and not to seek Clearance then there are limited opportunities for the Trustees to engage on what they might see as material detriment.

This reluctance to seek Clearance is perhaps due to the perception based on experience that, regardless of the merits of mitigation agreed between an employer and trustee, if Clearance is requested, the Pensions Regulator will always demand more.

It would be helpful to rebuild confidence in the Clearance regime, for example by allowing Trustee applications or joint Trustee-Employer applications. This would be most effective if the parties have confidence that the Pensions Regulator will accept outcomes agreed between the Employer and Trustee that lie within a realistic corridor of professional judgement.

22 Should anything else be considered?

Please provide your comments in the box below:

Corporate Transaction Oversight - Engagement With Other Regulators

Improved Regulator Powers - Introduction

Improved Regulator Powers - Our Proposals

Improved Regulator Powers - Who Will Be Penalised?

Improved Regulator Powers - Questions

23 What are the likely effects and impacts on business and trustees of the introduction of this proposed new system of penalties?

Please provide your comments in the box below:

There should be no direct impact on well-run schemes and responsible employers. For the less good, the flow of information should improve as should the proper engagement of professional advisers. An indirect consequence could be that it becomes more difficult to attract trustees to undertake roles which carry such penalties. In relation to Trustees, more power should be afforded to Trustees to require employers to provide information (or permit tPR to disclose information provided under s72) in order to enable Trustees properly to carry out their duties.

24 Are there other behaviours that should attract sanctions? If so, what are they?

Please provide your comments in the box below:

We note that the proposed new sanctions will have to take into account the provisions of s226(3) of the Pensions Act that a recovery plan must comply with any prescribed requirements and must be appropriate having regard to the nature and circumstances of the scheme.

25 We have proposed a new civil penalty (up to a maximum £1m) for example to take action for non-compliance with providing a declaration of intent. Will this deter wrongdoing? If not, what would be a suitable deterrent?

Please provide your comments in the box below:

We are not in a position to say whether this will deter wrongdoing until the use of such penalty has been seen in practice. The likelihood of the penalty being imposed and the size of the fine will both be factors and, relative to pension obligations, £1 million will generally not be significant, so it may be appropriate to make the cap proportionate, for example to the s75 debt. We note that other regulators have powers to impose significantly higher penalties (for example the Information Commissioner).

Where any wrongdoing is carried out by a sponsoring employer or a company in which it has a direct or indirect interest, any penalties that are not 'additional contributions' to the scheme, would potentially further weaken the employer covenant available to the scheme. All such penalties should therefore be paid into the scheme.

It is unclear however that Directors duties to pension schemes should be any more or less onerous than their fiduciary duties to all other stakeholders e.g. employees, creditors etc, other than for overtly political purposes.

26 We have proposed a new criminal offence for wilful or reckless behaviour in relation to a pension scheme, and for failures to comply with Contribution Notices and the Notifiable Events Framework. Do you agree with these proposals? Will they deter wrongdoing? If not, what would be a suitable deterrent?

Please provide your comments in the box below:

27 If yes, should the maximum penalty for these offences be: Unlimited fines? Custodial sentence and/or fine for the worst offenders – do you have views on the appropriate maximum term?

Please provide your comments in the box below:

28 What more can we do to support the Pensions Regulator in enforcing legal requirements in an effective and proportionate way?

Please provide your comments in the box below:

Anti-avoidance - Introduction

Anti-avoidance - Our Proposals

Anti-avoidance - Questions

29 We have set out a number of proposed changes to the way Contribution Notices function. Do these proposals strike the right balance between improved regulations on business and protecting pensions?

Please provide your comments in the box below:

The proposals appear reasonable. The current restriction to level of benefit received by the target could be argued to make it a "no lose" gamble by a wrongdoing employer i.e. pay £x now, or pay nothing now, with the threat of only paying £x if it gets caught. The penalty for wrongdoing must be substantially greater than the original benefit gained by the employer / loss suffered by the scheme. This would be even more fair if the Regulator engages pre-transaction and the wrongdoing employer ignores the Regulator's direction given during that pre-transaction period.

30 Alternatively, what else could we do to improve the way Contribution Notices work?

Please provide your comments in the box below:

31 What would be the most appropriate way of protecting the value of the Contribution Notice through uprating? What are the likely impacts of this?

Please provide your comments in the box below:

As this would only apply in circumstances where wrongdoing has taken place, any reasonable method of uprating would be acceptable. This should lead to better recoveries to the scheme and might remove another incentive for a wrongdoer to delay making payments. Any new legislation should reconcile with the Insolvency Act and be clear on the treatment of any uprating, where the target is, or becomes, insolvent, as under insolvency law claims are frozen at the date of insolvency.

32 What could be the impacts of changing the date at which the cap was calculated to a date closer to the final determination?

Please provide your comments in the box below:

As this would only apply in circumstances where wrongdoing has taken place, any reasonable method of cap calculation would be acceptable. This should lead to better recoveries to the scheme, and might remove another incentive for a wrongdoer to delay making payments. Any new legislation should reconcile with the Insolvency Act and be clear on the treatment of any updating, where the target is, or becomes, insolvent, as under insolvency law claims a frozen at the date of insolvency.

33 What would be the likely impacts on business of a more streamlined Financial Support Direction regime?

Please provide your comments in the box below:

Any measures that provide clarity around FSD would be welcomed by all parties.

34 How could we best amend the ‘insufficiently resourced’ test to make it simpler and clearer?

Please provide your comments in the box below:

Any measures that provide clarity around FSD would be welcomed by all parties. One option would be to prospectively simplify the trigger and base this on funding being less than a reasonably objective basis such as a percentage of the s75 debt or gilts basis and to dispense with the insufficiently resourced test; but equally the measure needs to take into account that different schemes invest and are supported in different ways (for example contingent asset support).

35 We propose to tighten up the forms of financial support the target is required to make to the scheme to include cash payments or statutory guarantees. What would the impact of this approach be on business?

Please provide your comments in the box below:

Any measures that provide clarity around FSD would be welcomed by all parties. A simpler approach would be to restrict initial Directions to cash but allow any appropriate counter-proposal to be acceptable, subject to the agreement of the trustees and the Pensions Regulator.

36 Are there other forms of support we should take into consideration?

Please provide your comments in the box below:

37 What would be the impact on business of a longer lookback period?

Please provide your comments in the box below:

Conclusion

Conclusion - Questions

38 The proposals in this consultation are suggested as ways in which the Pensions Regulator’s powers could be increased or improved in order to clamp down on corporate wrongdoing and ensure improved compliance with all legal responsibilities by sponsoring employers. Do these proposals strike the right balance between improved regulations on business and protecting pensions?

Please provide your comments in the box below:

It would assist in a restructuring and insolvency context if the proposals could provide clarity about the status of insolvency claims and interest pending settlement in the context of Contribution Notices and Financial Support Directions.

39 Alternatively, do you think there are other areas where the Pensions Regulator’s powers could be increased or improved to achieve our intended outcomes?

Please provide your comments in the box below: