HERBERT SMITH FREEHILLS

Pensions

SEPTEMBER 2019

Although Brexit will have little immediate impact on pension law and regulation in the UK, pension scheme sponsors and trustees should take immediate steps to assess the potential impact of Brexit on the sponsors' business and the scheme. It is critical that they prepare for all eventualities and ensure that contingency plans are in place to protect against material risks.

Three key risks that trustees and sponsors need to assess and, where possible, mitigate are the potential impact of Brexit on:

- the sponsor's business and financial strength
- scheme investments
- scheme funding and security arrangements.

As Brexit unfolds, trustees and sponsors should also work together to consider whether the balance of their scheme's funding, covenant and investment risk remains appropriate.

Impact on sponsor

Pension scheme sponsors need to assess the potential impact of Brexit, whatever form it takes, on their business and its financial position. In particular, they need to understand the potential impact on their business of market volatility, changes to trading patterns, disruption to supply chains and changes to immigration rules. The potential impact of changes in the political landscape should also be assessed. Contingency plans should be put in place to address all material risks.

Pension scheme trustees should engage with their scheme's sponsor to understand the potential impact of Brexit on the sponsor's business and how this may affect its support for the scheme. Trustees should also ask for details of the contingency plans that are in place to address any major risks to the sponsor's business.

Impact on scheme investments

The ups and downs of the Brexit negotiations and the resulting political fallout has already resulted in significant market volatility. This is likely to be compounded in the event of a no-deal Brexit. The economic impact of Brexit could also affect asset values and investment returns.

Trustees of defined benefit schemes should take advice on the potential impact of Brexit on their scheme's investment strategy and what steps they might take to mitigate downside risks.

Trustees of defined contribution schemes should review the investment funds that are

The section is part of our Brexit Legal Guide.

No deal

- If the Withdrawal Agreement endorsed by the EU Council on 25 November 2018 or the Political Declaration, or some version of both, are not approved by 31 October 2019 and there is no change to the exit date, the UK will cease to be a member state on that date without any transitional period
- Sponsors and trustees should assess the potential impact on scheme funding and security arrangements, investments and the sponsor's business and ensure contingency plans are in place
- There would be no material changes to the rules governing workplace pension schemes, including those relating to scheme funding, governance requirements, data protection, equal treatment and the protection of members on insolvency
- Existing contracts may need to be amended to allow personal data to continue to be received from organisations or data centres within the EU

available to members and consider whether they remain appropriate in light of any material risks to members' funds.

Impact on scheme funding and security arrangements

Market volatility and the economic impact of Brexit may impact the funding level of defined benefit schemes. Sponsors and trustees should consider how this may impact funding and security arrangements that are in place. For example, contingent payments under funding or security arrangements may be triggered where a scheme's deficit increases or there is a weakening in a sponsor's financial position. The impact of any contingencies being triggered on the sponsor's business should also be assessed.

No-deal – additional issues

Payments to members who live in an EU27 member state

Concerns have been raised about the ability of UK insurers to make payments to individuals living in an EU27 member state in the event of a no-deal Brexit. However, many insurers are putting in place contingency plans to enable them to continue to make these payments, where possible. In addition, certain member states have indicated that they will continue to allow payments from UK insurers after Brexit, notwithstanding that the issue may not have been resolved as a matter of law. Therefore, it is hoped that any disruption to payments would be minimal.

Occupational pension schemes are not subject to the same rules as insurers in relation to payments within the EU. Accordingly, there is no reason why UK occupational pension schemes should be prevented from making such payments.

There may also be difficulties for individuals living in the EU27 accessing services from UK banks after the UK ceases to be part of the Single European Payments Area. This could impact the ability for these individuals to access their pension benefits where they are paid into a UK bank account. However, UK banks are alive to this issue and so we would expect a solution to be found in the event of a no-deal Brexit.

> "The biggest Brexit related risks for pension schemes are the impact on their sponsor and the wider economy."
>
> **SAMANTHA BROWN**

Sending personal data to the EU

The UK Government has confirmed that in recognition of the unprecedented degree of alignment between the UK and EU's data protection regimes, the UK would, at the point of exit, continue to allow the free flow of personal data from the UK to the EU. However, it plans to keep this under review. The UK Government also plans to recognise EU adequacy decisions made with third countries (eg Japan) prior to our exit.

Receiving personal data from the EU

The European Commission has stated that if it deems the UK's level of personal data protection essentially equivalent to that of the EU, it would make an adequacy decision allowing the transfer of personal data to the UK without restrictions. However, the Commission has said that a decision on adequacy cannot be taken until the UK is a third country and it is unclear how long it will be before any decision is made.

If the European Commission does not make an adequacy decision at the point of exit and schemes or other organisations want to receive personal data from organisations established in the EU (including data centres), then they will need to work with their EU partners to identify a legal basis for those transfers. In most cases, this will require standard contractual clauses to be put in place.

Relevant no-deal guidance

- Benefits and pensions for UK nationals in the EU, EEA or Switzerland if there's a no-deal Brexit
- Banking, insurance and other financial services if there's a no-deal Brexit
- Workplace rights if there's a no-deal Brexit
- Data protection it there's a no-deal Brexit.

- Several draft regulations have already been published, which would make minor consequential amendments to pensions legislation, including the Pensions Act 1995, the Pension Protection Fund Entry Rules 2005 and the Occupational Pension Schemes (Investment) Regulations 2005
- There would be scope for the UK to deviate from EU rules over time, although the Government has given no indication so far that it plans to do this

Deal/transitional period

- If approved by the UK Parliament, the Withdrawal Agreement, or some version of it, will set out arrangements for the UK's withdrawal from the EU – when the UK will cease to be a member state
- A transition period will follow the date of the UK's EU exit up till at least the end of 2020, possibly the end of 2021 or 2022
- If this or a similar agreement is put in place, it would mean that:
  - directly applicable EU legislation such as the IORP II Directive and the General Data Protection Regulation would continue to apply
  - CJEU judgments would continue to apply in the UK
  - there will not be any immediate changes to the UK's pensions legal and regulatory regime
  - the extent to which future EU laws relating to pensions apply to UK schemes would be determined by the agreement on the UK's future relationship with the EU
  - any attempts to reduce or amend regulatory requirements on schemes or sponsors post-Brexit may be impacted by the agreement on the future relationship

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