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Pensions Regulator Outlines Scope of New Pensions Criminal Offences but Uncertainty Remains

Samantha Brown, Partner, and John Whiteoak, Partner, Herbert Smith Freehills LLP, London, UK

Synopsis

The Pensions Regulator draft policy on its approach to investigating and prosecuting the new criminal offences to be introduced this Autumn under the Pension Schemes Act 2021 sets out:

- how the Regulator will select cases for investigation and prosecution
- the factors the Regulator will take into account in assessing whether a person has a ‘reasonable excuse’ for their conduct
- examples of the circumstances in which the Regulator might bring a prosecution.

This guidance has been produced in response to concerns that have been expressed about the scope of the new offences which cover a wide range of corporate activity and which apply to any person (including directors, lenders, investors, trustees and advisers) who commits a relevant act or engages in a relevant course of conduct (other than an insolvency practitioner acting in their capacity as such).

However, the guidance contains mixed messages and creates unnecessary uncertainty. It also does not cover the new financial penalties of up to £1 million which the Regulator will be able to impose on any person in any even wider range of circumstances or the two new contribution notice triggers. Therefore, while it provides some clarity, the policy is unlikely to be sufficient to mitigate the negative impact of the new powers on corporate activity and investment and on the scope to restructure businesses with DB schemes.

Background

The powers of the Pensions Regulator are due to be significantly increased this Autumn when Part 3 of the Pension Schemes Act 2021 comes into force. These new powers have been granted by Parliament

in response to the Regulator’s perceived weakness in responding to recent high-profile corporate failures involving companies with defined benefit (DB) pension schemes. Although the Government has indicated that these new powers are aimed at ‘wilful’ or ‘reckless’ conduct by directors and other parties which jeopardises the interests of a DB scheme, there has been widespread concern expressed about the scope of these new powers, which include:

- power to prosecute three new criminal offences related to conduct which negatively affects defined benefit (DB) pension schemes
- power to impose new financial penalties of up to £1 million in a range of circumstances
- two new triggers for contribution notices, and
- new and extended information gathering powers and reporting requirements.

Concern has also been expressed about the potential impact of these new powers on corporate activity in the UK, including on the scope to restructure businesses with DB schemes.

In response to this concern, the Pensions Minister promised that the Pensions Regulator would issue guidance outlining how it intends to use these new powers before they come into force. This guidance has now been published for consultation¹ in the form of a new policy setting out the Regulator’s proposed approach to investigating and prosecuting the new criminal offences.

The new offences

The draft policy recognises that the grounds for prosecuting a person under the new criminal offences are similar to the existing contribution notice triggers, applying (broadly) in relation to acts or failures to act which:

Notes

¹ <https://www.thepensionsregulator.gov.uk/en/document-library/consultations/consultation-on-our-approach-to-the-investigation-and-prosecution-of-the-new-criminal-offences>.

- are intended to avoid a debt arising under section 75 Pensions Act 1995 or to reduce the value of such a debt, or
- have a materially detrimental impact on the likelihood of benefits under a DB scheme being paid.

However, the policy also highlights some potentially important differences between the relevant statutory requirements including the fact that:

- the new criminal offences apply to *any person* (other than an insolvency practitioner acting in their capacity as such) and not just sponsoring employers and persons ‘connected’ or ‘associated’ with them
- no limitation period applies to the prosecution of the new criminal offences (in contrast to the six year limitation period that applies to contribution notices), and
- there is a higher burden of proof on the prosecutor in relation to the criminal offences compared with the imposition of a contribution notice.

In deciding whether the material detriment test is met for the purposes of the offence under section 58B, the Regulator indicates that it will take the same approach as when considering whether to issue a contribution notice on these grounds. In particular, it will take account of the matters set out in section 38A(4) of the Pensions Act 2004, Code of Practice 12 and the Code-related guidance which include:

- the impact of the act or failure on the scheme
- the impact of the act or failure on the scheme’s sponsoring employers and their ability to support the scheme
- the extent to which the act or failure may impact any person’s ability to discharge their obligations to the scheme, including on insolvency.

Reasonable excuse

Given the wide range of acts potentially covered by the new offences, in many cases the question of whether or not a criminal offence has been committed will turn on whether the relevant person(s) had a ‘reasonable excuse’ for their conduct. The legal burden will be on the prosecution to prove the absence of a reasonable excuse. However, in the Regulator’s view, this does not mean that the prosecution must identify and disprove every possible excuse open to someone.

The Regulator expects those it investigates to explain their actions and put forward sufficient evidence of any matters that might amount to a reasonable excuse and will give them the opportunity to do so. It also expects the basis for the reasonable excuse to be clear from contemporaneous records such as minutes of meetings, correspondence and written advice.

What amounts to a reasonable excuse in any particular case will be fact-specific. It will also ultimately be a matter for the Court or a jury to determine. However, for the purpose of determining whether or not it is appropriate to bring a prosecution, the Regulator indicates that it will take account of all relevant factors when assessing whether a person has a reasonable excuse for their actions. Within this, three factors which the guidance highlights as being of particular significance are:

- i whether the detrimental impact on the scheme/likelihood of full scheme benefits being received was an incidental consequence of the act or omission, as opposed to a fundamentally necessary step to achieve the person’s purpose
- ii the adequacy of any mitigation provided to offset the detrimental impact, and
- iii where no, or inadequate, mitigation was provided, whether there was a viable alternative which would have avoided or reduced the detrimental impact.

Selecting cases for investigation and prosecution

The Regulator makes clear that it will be mindful of the policy intent behind the new offences when selecting cases for prosecution meaning, for example, it will focus on circumstances where:

- the primary purpose of the conduct is the abandonment of the scheme without provision of appropriate mitigation
- significant financial gains have been unreasonably made to the detriment of the scheme
- there has been some other unfairness in the treatment of the scheme, and/or
- the trustees, the Regulator and/or the Pension Protection Fund have been misled or not appropriately informed.

The policy indicates that the type of behaviours the offence is trying to target are likely to be carried out by people with significant decision-making power, but this does not exclude the possibility of this behaviour being carried out, helped or encouraged by others who could also be prosecuted.

What actions might be caught?

The policy contains various examples of the sort of conduct that might be considered appropriate for prosecution. This includes the following scenarios which the Regulator has previously encountered:

- The sale of an employer without replacing an existing parental guarantee over the employer's section 75 debt, resulting in the loss of the guarantee (in circumstances where the trustees were not told about the sale in advance).
- The purchase of an employer with no further investment into its business, subsequent mismanagement of the company, and extraction of value before the company went into administration.
- The stripping of assets from an employer, which resulted in substantial weakening of the support for the scheme.
- Taking steps to bring about the unnecessary insolvency of a scheme employer with the intention of buying the employer's business without the scheme.

The Regulator's approach

The draft policy attempts to provide reassurance over the scope of the new criminal offences and the frequency with which prosecutions for these offences are likely to occur. The Regulator indicates that its approach to the prosecution of the new offences will be closely linked to its existing contribution notice power, in that it would expect to consider a case for prosecution in broadly the same circumstances where it would consider imposing a contribution notice. This is notable given how sparingly the Regulator has used its existing contribution notice powers. The policy also reiterates that the new offences are aimed at 'the more serious intentional or reckless conduct' and that they are not intended to 'achieve a fundamental change in commercial norms or accepted standards of commercial behaviour in the UK'.

However at the same time, the policy:

- fails to provide unequivocal assurance that an entity that has 'fully mitigated' the detriment to its scheme will not be prosecuted,
- stops short of saying that an entity which implements a court sanctioned Part 26A restructuring plan will always have a reasonable excuse, and
- provides no comfort to employers that have obtained clearance in respect of a transaction or particular corporate activity that they will not be prosecuted.

If, as indicated by the Pensions Minister and the Regulator, these offences are indeed aimed at the most egregious acts we would expect that criminal prosecution in these circumstances could be ruled out and it would be helpful if the final policy could go further in this regard to make this clear. Otherwise this creates unhelpful uncertainty, particularly in scenarios that are not so clear cut.

In addition, the examples included in the draft policy tend to sit at the ends of the spectrum – either falling clearly within the boundary of legitimate activity or clearly within the scope of the new offences. Most corporate activity will fall somewhere in between and more clarity is needed on how the new offences will be enforced in these 'middle ground' scenarios to enable persons in scope and their advisers to form a view about whether any proposed activity is lawful or not.

Scope of guidance

It is important to note that the draft policy:

- does not set out how the Regulator intends to use its new power to issue financial penalties of up to £1 million under section 88A Pensions Act 2004 (which applies in similar circumstances to the new offences as well as more broadly) or the two new contribution notice triggers, even though the Regulator is more likely to use these given the lower standard of proof associated with them, and
- will not apply to other authorities with the power to prosecute individuals or companies for these offences (namely, the Secretary of State and Department of Public Prosecutions in England, the Crown Office and Procurator Fiscal Service in Scotland and the Public Prosecution Service in Northern Ireland).

Once again, this leaves unhelpful uncertainty. To address this it is hoped that the Regulator will publish corresponding guidance on how, and in what circumstances, it might impose financial penalties under section 88A or make use of the new contribution notice triggers. It would also be helpful if the other prosecuting authorities would publicly endorse, or at least recognise, the Regulator's final policy or enter into a memorandum of understanding setting out the degree of consultation and co-ordination that would take place before any decision to prosecute is taken.

Retrospectivity

Although the Department for Work and Pensions and the Regulator have previously confirmed that these new powers will not be exercised retrospectively, the draft guidance indicates that the Regulator may take account of evidence which pre-dates the date on which these new offences come into force in the context of any investigation/prosecution of actions after that date, for example, if it indicates someone's intention. It is likely that such evidence might also be used (where relevant) to build a picture of whether or not a person has a reasonable excuse.

Conclusion

While the Regulator's draft policy gives some indication of the factors that it will consider in deciding how to police the new pensions criminal offences, it also creates unnecessary uncertainty by failing to provide reassurance that the offences will not apply in scenarios that seem to be well within the boundary of legitimate conduct and by failing to provide more commercially realistic examples. The policy also fails to address the questions and concerns related to the Regulator's new power to issue financial penalties of up to £1 million and its extended contribution notice powers, despite the fact that it is more likely to exercise these powers in practice.

It is to be hoped that the Regulator will address these points in its final policy, which is due to be issued before the new offences and regulatory powers come into force this Autumn. Although, even if it does, the introduction of these new sanctions will still take everyone that works with defined benefit schemes and their sponsors into new and uncomfortable territory.

While we would do not expect the Regulator to be gung-ho in its use of these new powers, there is no doubt that they will increase the threat that it poses. Even if the chances of being prosecuted are low, this increased threat in itself is likely to impact corporate behaviour. This is why it is so important that the Regulator's final policy is as clear and helpful as possible, particularly given that businesses and schemes are grappling with enough uncertainty at the present time as it is.

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