

REGULATOR ISSUES DRAFT GUIDANCE ON POLICING NEW CRIMINAL OFFENCES

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Legal Briefings

The Pension Regulator has published for consultation its much anticipated [draft guidance](#) on how it intends to police the new pensions criminal offences due to come into force this Autumn. The draft guidance suggests that the Regulator will use these new powers sparingly and that they are not intended to fundamentally change commercial norms or accepted standards of corporate behaviour. However, it also highlights the need for corporate decision-makers to be able to demonstrate how they have taken account of the interests of their defined benefit (DB) scheme (where relevant) and what, if any, mitigation has been put in place to protect the interests of their DB scheme where corporate actions have a materially detrimental impact on the scheme.

While the draft guidance provides some helpful insights into the factors the Regulator will take into account before deciding whether to prosecute an individual or company for one or other of these new offences, it is important to note that:

- the guidance 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), and
- the draft guidance does not set out how the Regulator intends to use its new power to

issue financial penalties of up to £1 million 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.

The consultation period closes on 22 April and the draft guidance hints that the new powers may come into force on 1 October 2021 (although to date the Pensions Minister has been less specific referring simply to "the Autumn").

For more background on the new offences read our [blog](#) on the new criminal offences to be introduced by the Pension Schemes Act 2021.

KEY TAKE-AWAYS

- The draft guidance suggests that prosecutions for these new offences are likely to be rare and that the Government did not intend to fundamentally change commercial norms or accepted standards of corporate behaviour in the UK.
- The guidance sets out a wide range of factors which the Regulator will take into account in determining whether to prosecute an individual or company and in assessing whether a person has a reasonable excuse for their actions, including the reasons for taking the action in question, the degree of harm caused to the scheme, the adequacy of any mitigation put in place, whether the scheme has been treated fairly and whether there was a viable alternative.
- The draft guidance highlights the importance of considering the impact of corporate activity on a DB scheme and the steps that could be taken to mitigate this and the importance of maintaining contemporaneous written records of this as part of the corporate decision-making process.

POLICY INTENT AND THE REGULATOR'S APPROACH

In the introduction to the guidance, the Regulator notes that:

"As the new legislation progressed through Parliament, ministers confirmed that the offences were not intended to achieve a fundamental change in commercial norms or accepted standards of corporate behaviour in the UK. Rather, we understand they were aimed at enabling us to address the more serious intentional or reckless conduct that was already within the scope of our contribution notice powers, or would be in scope if the person was connected with the scheme employer".

The guidance indicates that the Regulator's approach will be guided by its understanding of this policy intention. It also says that:

"We will use these powers where the seriousness of the behaviour warrants such intervention to further our statutory objectives and protect savers. Both the CN and the criminal offences have a deterrent effect. Whether we decide to use the CN or the criminal offences or both will be guided by the efficient use of our resources to deter repetition of similar bad behaviour and act as a warning to others".

The Regulator indicates that its approach to the prosecution of the new offences will be closely linked to its existing contribution notice (**CN**) power, in that it would expect to consider a case for prosecution in broadly the same circumstances where it would consider seeking a CN. This is notable given how sparingly the Regulator has used its existing CN powers. The guidance also notes that there may be circumstances where the Regulator will not pursue a CN (for example, where the target's resources mean the amount of recovery would be low) but would still consider prosecution as its deterrent effect might be in the public interest. It may also decide to pursue a CN but not prosecute the target.

Although the policy sets out the Regulator's interpretation of the new offences, it acknowledges that the courts will ultimately decide the correct interpretation of the law. The Regulator will update its policy over time to reflect court decisions in relation to the offences and its experience.

SCOPE

The draft guidance only covers the new criminal offences of avoiding a section 75 debt and causing a material detriment to a DB scheme. It does not cover the circumstances in which the Regulator would consider exercising its new power to issue a £1 million fine nor the two new CN triggers.

In respect of the use of the new power to issue financial penalties the draft guidance points to the Regulator's [existing policy on Monetary penalties](#). It is unclear whether the Regulator plans to update that guidance in light of the new and more sizeable financial penalties which it will be able to impose in the future.

NEW CRIMINAL OFFENCES

The draft guidance recognises that the grounds for prosecuting an individual under the new criminal offences are similar to the existing CN triggers. However, it 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.

MATERIAL DETRIMENT

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 CN on the grounds that an act or failure to act has caused a material detriment to a DB scheme.

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.

The Regulator would not usually expect to prosecute anyone under for the new criminal offence related to causing a material detriment where the person could establish a statutory defence to a material detriment CN.

REASONABLE EXCUSE

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. The Regulator will take account of all relevant factors, but there are three factors which the guidance highlights as being significant in determining whether there is a reasonable excuse for the act or omission:

1. 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
2. the adequacy of any mitigation provided to offset the detrimental impact, and
3. 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 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 Regulator will generally engage before it decides to prosecute for a specific behaviour.

In considering whether to prosecute someone, the Regulator will consider:

- their relationship, duties and proximity to the employer, the scheme, and the act or failure to act
- the extent of their involvement or influence, and
- any direct or indirect benefit(s) the person receives or is entitled to by reason of the act or failure to act.

The guidance 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 guidance 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 the scheme employer with the intention of buying the employer's business without the scheme.

INTERVIEWS UNDER CAUTION

Where there are grounds for the Regulator to suspect that a criminal offence may have been committed and the person's answers may be used as evidence in a prosecution, any discussion with the Regulator will be conducted in the form of an interview under caution which complies with the requirements of the relevant Code of Practice issued under the Police and Criminal Evidence Act 1984.

RETROSPECTIVITY

Although the DWP 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.

CONTACTS

If you wish to discuss how any provisions of the Pension Schemes Act 2021 may impact your scheme or organisation please contact one of our specialists below or speak to your usual Herbert Smith Freehills' contact.

To keep up to date with the latest on these new powers and our upcoming soundbites podcast series in which we will explore the practical implications of them, subscribe to our [UK pensions blog](#).

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KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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