CLIFFORD CHANCE

UK: PENSIONS UPDATE – JUNE 2018

1. New data protection regime comes into force

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The GDPR

The General Data Protection Regulation (**GDPR**) took effect in the UK and other EU Member States on 25 May, introducing a new regime for the protection of people's personal data.

In practice, if pension scheme trustees already had robust data protection measures in place, GDPR did not necessitate a complete overhaul of these. However, the new requirements of the GDPR meant that action in a few key areas was likely to be needed in most cases. (Please see the December and March editions of UK: Pensions Update for more details).

The Data Protection Act 2018

Shortly before the GDPR took effect, the UK's Data Protection Act 2018 was passed. The Act replaces the Data Protection Act 1998 and is designed to supplement the GDPR (as well as transposing the Law Enforcement Directive[1] into UK law). The Act also includes specific provisions relating to the duties, functions and powers of the Information Commissioner's Office; the UK authority responsible for overseeing and enforcing data protection compliance in the UK (**ICO**).

ICO registration

Under the old regime, most data controllers had to be registered with the ICO and pay a registration fee (to be renewed each year). There were some exemptions, but none of these applied to trustees of occupational pension schemes generally. The amount of the registration fee under the old regime depended on the controller's staffing size and financial turnover, meaning that the vast majority of pension scheme trustees would have fallen within the lowest charging tier – being required to pay a £35 annual registration fee.

There is no longer a requirement to register with a supervisory authority like the ICO under the GDPR. However, new UK regulations[2] came into force on 25 May, under which data controllers are required to provide some basic information and pay a charge to the ICO (in a similar way to the old regime). The charging structure has changed slightly, but it is again expected that the vast majority of pension scheme trustees would fall within the lowest bracket (tier 1) – requiring a £40 fee (or £35, if paying by direct debit). This obligation will continue to apply annually.

For controllers who are already registered, the obligation will not apply until their existing registration/fee expires (i.e. 12 months after their most recent registration/fee was made) and registration status can be checked on the ICO's website.

The ICO's guidance issued earlier this year (when the regulations were still in draft) said that the ICO would write to controllers who are already registered before their registration expires and explain what they need to do next.

[1] *EU Data Protection Directive 2016/680.* This governs the processing of personal data for law enforcement purposes.

[2] *The Data Protection (Charges and Information) Regulations 2018.*

Trustees should therefore check their registration status and, if they have not heard anything from the ICO, follow-up before their current registration expires.

The Pensions Regulator's cyber risk guidance

The Pensions Regulator recently published new guidance for pension scheme trustees as a good practice guide to those steps which should be taken to protect against 'cyber risk' - the risk of loss, disruption or damage to a scheme or its members as a result of the failure of IT systems and processes.

Compliance with the new regime

Data protection is, of course, not a 'tick-box' exercise and just because 25 May has now been and gone, does not mean that it can be forgotten about. A key focus of the new regime is on accountability and being able to demonstrate self-compliance – trustees should therefore be mindful of this and ensure their privacy policies are kept under regular review.

2. Upper Tribunal upholds Regulator's issue of Financial Support Directions in ITV/Box Clever case

Last month, the Upper Tribunal handed down its decision in the *ITV/Box Clever* case;[3] concluding that the Regulator did have jurisdiction and that it was reasonable for the Regulator to issue Financial Support Directions (**FSDs**) to five ITV companies in this long-running anti-avoidance case.

This was the first anti-avoidance case to be heard in full by the Upper Tribunal and it provides some useful insight into how the Tribunal views the various elements of the test which need to be met for the issuance of an FSD. It is, however, understood that ITV intends to appeal the decision, so there may be more to come on this.

Background

The case related to a determination made by the Regulator's Determinations Panel in December 2011 to issue FSDs against five companies in the ITV group (the Targets) requiring them to provide financial support to the Box Clever Group Pension Scheme.

The Regulator's case was based on the Targets' involvement in a joint venture which took place between 1999 and 2003 and involved the merger of the TV rental businesses of the Granada group and the Thorn group.

The Targets challenged the Regulator's issuance of the FSDs on the basis that the Regulator did not have jurisdiction to issue the FSDs, or failing this, it was in any event not reasonable for the Regulator to issue the FSDs.

Jurisdiction issues

Lack of association

- The Targets argued that they were not "connected" with or "associates" of the employers in the pension scheme at the relevant time. (The tests to fall within scope of the Regulator's powers).
- The Tribunal held that this was a technical test to be applied by the application of the statutory provisions. This meant that the question as to whether a person is "*entitled to exercise, or control the exercise*" of the relevant voting power (relevant to the connected/associated tests) was not to be determined by the extent to which the Targets *actually* influenced the way any of the companies within the Joint Venture carried on their business.

Retrospectivity

- The Targets argued that the power to issue an FSD in section 43 of the Pensions Act 2004 did not operate retrospectively and all the facts regarding the conduct of the Targets occurred before section 43 came into force.
- The Tribunal held that section 43 is not retrospective legislation. It is concerned with looking at the current situation, but the current situation may well have arisen because of the way in which the scheme employers and those connected/associated with them had been run historically. The Regulator was not precluded from taking into account

[3] *ITV plc and others v The Pensions Regulator [2018] UKUT 0164 (TCC).*

events and transactions that took place some time before the power came into force, to the extent relevant to the current situation.

Discriminatory treatment

- The Targets argued that the decision of the Regulator to pursue the Targets, but not to pursue the other Joint Venture partner was discriminatory.
- The Tribunal held that to treat like cases differently *without* an objective justification is arbitrary and therefore disproportionate and unreasonable. However, the strength of justification needed depends on the strength of the expectation of equal treatment. In this case, there is no requirement in section 43 that the Regulator must pursue every person who at the relevant time falls within scope, although as the Targets and the other Joint Venture partner were the only real candidates, some objective justification was needed for deciding to pursue one and not the other.
- The Tribunal decided there was sufficient objective justification for the difference in treatment here. In particular, there had been no express indication at any time by the Regulator to the Targets that it would take the same decisions as regards the Targets as against the other Joint Venture partner.

Absence of moral hazard

- The targets argued that for section 43 to be engaged, it was necessary to identify behaviour which was in some sense 'morally hazardous' and there had been no such behaviour on the Targets' part.
- The Tribunal held that the FSD provisions in the legislation lay down in detail the test which must be satisfied before the Regulator has jurisdiction to issue an FDS. These clearly do not include any requirement that the conduct of the potential targets needs to have been such as to create the moral hazard at which the regime is directed.

Reasonableness issues

The Tribunal made a general comment that the three previous FSD cases of *Sea Containers*, *Nortel* and *Lehman Brothers* did not provide assistance here, making clear that the issue of reasonableness must be carefully considered in light of all the relevant circumstances of the particular case (and previous decisions are therefore likely to be of limited value).

The key factors considered:

- **The relationship between the Targets and the employers:** it was clear from the decision that the closeness of the relationship between the Targets and the scheme employers was key, with the Tribunal commenting that "*the closer the relationship is or has been the more likely it will be that it will be reasonable to issue an FSD*". The more distant the relationship, the less likely it would be reasonable to issue an FSD, even if the potential target has received benefits from the employer. The Tribunal concluded that the Targets exercised close control in practice over the operations of the Joint Venture.
- **The benefit received directly or indirectly by the Targets from the employers:** The Tribunal held that the Targets had received several benefits through the creation of the Joint Venture, including immediate cash realisation of their interest in a declining business, which was considered a valuable benefit.
- **Connection with the scheme:** The Tribunal held that the Targets were closely involved in the decision to establish the pension scheme.
- **Financial circumstances of the Targets:** The Tribunal did not view this to be relevant in this case. It was common ground that the Targets have the funds to comply with any direction imposed, but this should not be a point in favour of issuing an FSD – "*in a case where potential targets are sufficiently resourced, financial circumstances should be regarded as a neutral factor.*"

3. Work and Pensions Committee launches inquiry into Pensions White Paper

The Select Committee has launched an inquiry into the Government's White Paper on defined benefit (**DB**) pensions.

The White Paper was published in March and sets out a number of proposals for reforms to the regulation of DB schemes, including: (i) strengthening rules in certain areas to support/enhance the existing regime and introducing new powers to punish those who deliberately put schemes at risk: (ii) producing a revised DB funding code; and (iii) developing models to encourage consolidation of DB schemes (please see the March edition of UK: Pensions Update for more details).

The inquiry is designed to inform and influence future consultations on the proposals set out in the White Paper and numerous submissions in response to the inquiry have been published, with the proposals for DB consolidation (and the creation of so-called 'superfunds'), in particular, receiving much attention.

The deadline for submitting responses to the inquiry has recently passed (18 May) and it remains to be seen what the outcome will be.

4. Final master trust regulations are laid before Parliament

Following the Department for Work and Pensions (**DWP**) consultation (please see the March edition of UK: Pensions Update for more details), the regulations governing the regime for regulating master trusts have now been laid before Parliament. They are due to come into force on 1 October 2018.

Current status

The Pension Schemes Act 2017 introduced the new regime for master trust regulation and received Royal Assent last year. However, most of the Act[4] is not yet in force and the remaining provisions, along with the new *Occupational Pension Schemes (Master Trusts) Regulations 2018*, are due to come into force from 1 October this year.

Existing master trusts will have until April 2019 to apply for authorisation. The Regulator is allowing schemes to voluntarily submit a draft authorisation application between 1 May and 15 June for feedback (Schemes will still need to submit a formal application from October).

Scope

The framework applies to "master trusts" as defined under the Act. Broadly, a private sector occupational pension scheme that is used/intended to be used by two or more unconnected employers to provide defined contribution (**DC**) benefits (either alone, or in addition to other benefits) and which is not a relevant public service pension scheme. (In a scheme providing DB and DC benefits, the application for authorisation only needs to cover the DC aspects of the scheme (subject to certain limited exceptions)).

The Regulations will also exempt some schemes from the scope of the regime, including: (i) DB schemes only offering DC benefits which are AVCs or related to transfers-in from active DB members; (ii) the scenario where, following a corporate restructuring, scheme members remain temporarily in their original pension scheme while employed by an outside (i.e. otherwise unconnected) employer; (iii) certain schemes originally established as DB only which have a closed membership and whose membership is limited to members/former members of a pension scheme established by statute for a specific occupational group, industry or profession – designed to catch schemes in privatised sectors; and (iv) small self-administered schemes where 50% or more of the trustees are members.

Authorisation requirement

- Section 3 of the Pension Schemes Act 2017 will impose a prohibition on operating a master trust scheme unless the scheme is authorised.
- To gain authorisation, the trustees will need to apply to the Regulator. Existing master trusts must apply within 6 months of the prohibition coming into force (i.e. by April 2019). The application fee will be £23,000 for new schemes and £41,000 for existing schemes (to reflect the view that more work will be required to process existing scheme applications).
- The Regulator will then decide whether it is satisfied that the scheme meets the 'authorisation criteria'. The Regulator also has wide discretion to "*take into account any matters is considers appropriate*". The Regulator has 6 months to make its decision from the date it receives the application.

The authorisation criteria

- The persons involved in the scheme are fit and proper persons.
- The scheme is financially sustainable.

[4] Some of the provisions in the Act came into force on 27 April last year, which relate to existing master trusts in operation before 1 October 2018. Namely, these relate to the requirement to notify the Pensions Regulator that a triggering event has occurred.

- The scheme funder meets specified requirements.
- The systems and processes used in running the scheme are sufficient to ensure that it is run effectively.
- The scheme has an adequate continuity strategy.

Ongoing supervision and triggering events

- The Regulator is to supervise master trusts on an ongoing basis and if it stops being satisfied that an authorised master trust meets the criteria, it may withdraw authorisation.
- The Act sets out various triggering events, including: (i) withdrawal of authorisation; (ii) an insolvency event occurring in relation to a scheme funder; and (iii) the master trust being wound up.
- If a triggering event occurs, the trustees must either transfer out the benefits to another scheme and wind-up the original one (continuity option 1); or 'resolve' the triggering event (continuity option 2), depending on the type of event. The Regulator will have power to 'pause' certain master trust activities once a triggering event has occurred (including the acceptance of new members and payment of benefits).

Future developments

The Regulator is currently consulting on a draft Code of Practice (which covers the procedure it expects to follow when deciding whether to grant authorisation). The consultation is also asking for views on what should be included in the accompanying guidance, to be published separately. Consultation on the Code closed on 8 May.

5. Select Committee publishes report following inquiry into pension freedoms

The Work and Pensions Select Committee published a final report follows its inquiry into the pension freedoms (i.e. DC flexibilities) in April.

It reported findings that people are not engaged enough with and are making uninformed decisions about accessing their retirement savings and the report sets out a number of recommended changes to the pensions framework, as summarised below.

At this stage, they are simply recommendations and it remains to be seen what action the Government may take in response. (It is also noted that the details/scope of how some of the proposals would work are currently unclear, particularly regarding the default decumulation pathway).

Protecting savers

- **Introduction of a "default decumulation pathway":** Following the success of automatic enrolment which works on a passive basis, the Committee feels a similar approach should be taken to the decumulation phase (i.e. accessing pension savings) instead of requiring individuals to make an active choice.

  Recommendation: The Government should require any provider offering drawdown to offer a 'default decumulation pathway' that is targeted at their 'core customer group'. If an individual does not make an active choice at retirement, they would automatically be moved into the default product. IGCs should also be required to scrutinise the value for money offered by the default decumulation product. To be in place by April 2019.

- **Extension of NEST to provide decumulation products:** NEST may drive better retirement outcomes by forcing other providers to offer greater value if it were to offer its own decumulation products.

  Recommendation: The Government should allow NEST to provide decumulation products (both annuities and drawdown), including a default drawdown pathway (as above). From April 2019.

Empowering savers to choose

- **Requirement to produce one-page "pension passports":** There is a clear consensus on the need to increase engagement with pensions well before retirement. The suggestion of a mid-life "MOT" at age 50 (whereby individuals would review their financial health at an age where it's still possible to take action if they haven't been saving enough) was acknowledged as a good idea, but not one which would be likely to significantly change consumer behaviour. Current retirement wake-up packs are too long and detailed and members are not reading then.

Recommendation: The FCA and tPR should require all pension providers to issue one-page pensions passports as part of their pre-retirement communications with members. A template best practice passport should be produced this month.

- **Introduction of a single pensions dashboard:** The Government has previously committed to introducing a pensions dashboard (whereby consumers will be able to view information about all their pension entitlements in one place) by 2019. However, there have been suggestions that this may take the form of multiple dashboards hosted by different providers. Rather than doing this, it would be simpler just to have one dashboard.

  Recommendation: The Government should introduce a single pensions dashboard to be hosted by the new single financial guidance body (and funded by an industry levy). To be in place by April 2019.

- **Extension of dashboard to cover full range of pension provision:** For the dashboard to be of use, it needs to cover the full range of a consumer's pension entitlements i.e. state pension, DB and DC pensions.

  Recommendation: The Government should require all pension providers to provide necessary information to the pensions dashboard. To enable smaller legacy DB schemes sufficient time to comply, the Government should consult with the Pensions Regulator on an implementation timetable. The implementation timetable should ensure that at least 80% of all DB pensions are visible on the dashboard by April 2019, with the remainder to follow.

- **The introduction of automated advice**: While there is scepticism over its reliability, there is a clear role for automated services in providing cheaper advice.

  Recommendation: The Financial Conduct Authority should conduct and publish a review comparing consumer outcomes from face-to-face advice with those from automated advice. No timing specified.

6. The Regulator's corporate plan

The Pensions Regulator has published its corporate plan for 2018-21, setting out its priorities for the next three years.

The Regulator says that it is working to become a "clearer, quicker and tougher" regulator and it will focus on delivering the following priorities:

- Enhancing and executing effective regulatory approaches across all schemes – the Regulator is developing different regulatory tools to enable it to intervene more effectively and efficiently.
- Promoting good trusteeship though improving governance and administration – this will include a review and consolidation of the Regulator's existing guidance on governance standards and record-keeping to make its expectations clearer. The Regulator will also be working with the government and industry on the implementation of the pensions dashboard.
- Effective regulation of DB schemes – the Regulator will focus particularly on those schemes which 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.
- Effective regulation of master trusts – the Regulator will be delivering the new authorisation and supervision regime of master trusts from October 2018, commenting that it will also continue to engage with master trusts before they apply for authorisation.
- Ensuring employers meet their automatic enrolment duties – the Regulator will continue to focus on ensuring pension contributions are paid to schemes on time and in line with the contribution rate changes as they come into effect.
- Preparing for the impact of Brexit – the Regulator will work closely with the government and wider pensions industry to understand and respond to the potential effects of Brexit on schemes. It will also provide specific guidance to schemes and the industry where appropriate.
- Equipping the Regulator's people to meet the challenges it faces.
- Delivering the Pensions Regulator of the future – the Regulator is working to develop an approach to regulation that focuses on more proactive and targeted work.

7. Financial Guidance and Claims Bill passed

The Bill received Royal Assent on 10 May, becoming the Financial Guidance and Claims Act 2018.

Amongst other things, the Act:

- provides for the creation of a new financial guidance body to replace The Pensions Advisory Service, Money Advice Service and Pension Wise. The new body will provide pensions guidance, debt advice, money guidance and consumer protection;
- provides for the FCA to make rules for personal pension providers and the Secretary of State to make regulations for trustees of occupational pension schemes requiring each respectively to refer members to "appropriate pensions guidance" when they receive any application from a beneficiary to take or transfer their scheme benefits. Before proceeding with the application, the provider/trustees must check that the beneficiary has either received the guidance or opted-out of receiving it;
- enables regulations to be made to ban pensions cold-calling.

The provisions relating to (i) and (ii) are not yet in force.

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