UK PENSION SCHEMES ACT: LENDERS BEWARE

On 11 February 2021, the Pension Schemes Bill received Royal Assent and became the Pension Schemes Act 2021 (the "Act"). One of the key changes introduced by the Act in relation to defined benefit pension schemes is a new criminal offence for anyone engaging in conduct that detrimentally affects in a material way the likelihood of accrued scheme benefits being received. There are no specific exceptions for lenders or loan transactions where there is a defined benefit pension scheme in the borrower group. So, lenders need to become familiar with the new regime and be able to navigate the risks posed. The new offence is not yet in force (expected to occur at some point this year) and it is hoped that Pensions Regulator guidance soon to be consulted upon will offer some insights into the types of circumstances in which it expects to use its new powers. Despite some positive sound bites already from the Regulator that it will use its powers sparingly, the powers in the Act are drafted widely. Now the Act has Royal Assent it's a good time for lenders to take stock of the new regime and what happens next, which we touch on below.

Key issues

- The Pension Schemes Bill has received Royal Assent
- It introduces a new criminal offence in relation to defined benefit schemes for anyone engaging in conduct that detrimentally affects scheme benefits
- The new offence is anticipated to come into force at some point this year
- The Pensions Regulator is to consult on guidance shortly
- The guidance will be key in providing some indication on how the Regulator will use its new powers

THE NEW OFFENCE

Engaging in conduct that "detrimentally affects in a material way the likelihood of accrued scheme benefits being received"	
Offence	A person, if prosecuted, will be guilty of an offence where (on a criminal burden of proof) they: (a) do an act or engage in a course of conduct (including a failure to act) that detrimentally affects in a material way the "likelihood" of accrued scheme benefits being received; (b) they knew or ought to have known that the course of conduct "would" have that effect; and (c) they did not have a "reasonable excuse" for engaging in such conduct.
Penalty	A maximum custodial sentence of up to 7 years and/or a fine (unlimited) or new civil penalty up to £1m.

KEY CONCERNS FOR LENDING TRANSACTIONS

The key concerns for lending transactions are set out in the text box. The wide scope of the new offence combined with the severe penalties mean that there is some level of risk for anyone dealing with a group with a defined benefit pension scheme. Lenders should therefore be on notice when dealing with such a group and may need to consider the impact of any lending or restructuring transaction on the defined benefit pension scheme (e.g. if they are taking any security which ranks ahead of the scheme).

PENSIONS REGULATOR GUIDANCE

The Pensions Regulator will issue guidance prior to the new offence coming into force (which is expected to occur at some point this year) and will consult on the draft guidance first. It is hoped that the guidance will bring some much-needed clarity to the otherwise wide scope of the new offence, although the guidance will not be legally binding. In particular, it is hoped that the guidance will provide specific examples of where the Regulator would not expect to use its powers, including in relation to ordinary commercial lending and restructuring transactions (and/or for transactions where clearance has been sought). In the current economic climate this would be particularly welcomed. This would be in keeping with the government's stated aims of targeting wilful or reckless behaviour only and the intention not to interfere with normal business activity. Nevertheless, the question remains as to how much reliance can be placed on the guidance and any clearance process that is followed. Ultimately it will be for the courts to decide whether an offence has taken place and, if so, the appropriate sanction, including potential custodial sentences.

WHAT'S NEXT?

Whether the guidance will be the panacea for lenders remains to be seen. It may well turn out to be a case of déjà vu evoking the moral hazard regime introduced by the Pensions Act 2004 where lenders' initial concerns were subsequently assuaged by guidance issued by the Regulator. The new offence is anticipated to come into force at some point this year (and it is not expected to have retrospective effect) but lenders should start to seek appropriate advice on the potential risks they are likely to encounter. Fundamentally, it is not in anyone's interests (including trustees and beneficiaries) to discourage lenders from providing finance to groups with defined benefit pension schemes.

Key concerns for lending transactions

- **Low bar** - the threshold for detrimental conduct is low. There are many genuine circumstances in which an act may detrimentally affect the "likelihood" of scheme benefits being received e.g. taking on additional company debt
- **Scope** – the offence has broad application. It applies to *anyone* engaging in the detrimental conduct, which could include lenders
- **Reliance on the reasonable excuse defence** - what constitutes a reasonable excuse is unclear and will depend on the circumstances. For example, is there a reasonable excuse if a lender seeks to enforce a loan to a group with a defined benefit pension scheme where this is likely to have an adverse effect on the scheme? Would lenders be confident relying on the defence against the backdrop of criminal sanctions?

C L I F F O R D
C H A N C E

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