Phil Aspin
Chairman
The 100 Group Pensions Committee

E-mail: pensions@the100group.co.uk

Camelia Thomas
Secretary
GC100

Defined Benefit: The Pensions Regulator Powers team
DWP Consultation Coordinator
4th Floor
Caxton House
Tothill Street
London
SW1H 9NA

By email to: pensions.consultations@dwp.gov.uk

27 October 2021

Dear Sir/Madam

Response to consultation on Strengthening The Pensions Regulator's Powers: Notifiable Events (Amendments) Regulations 2021

We are writing on behalf of the Pensions Committee of the 100 Group of Finance Directors and on behalf of GC100 with regard to the above-named consultation.

About the 100 Group

The 100 Group represents the finance directors of the FTSE 100, several large UK private companies and some UK operations of multinational groups. Our member companies represent the vast majority of the market capitalisation of the FTSE 100, collectively employing 6% of the UK workforce, and in 2019 paid, or generated, taxes equivalent to 12% of total UK government receipts. Our overall aim is to promote the competitiveness of the UK for UK businesses, particularly in the areas of tax, reporting, pensions, regulation, capital markets and corporate governance.

The 100 Group represents companies sponsoring defined benefit (DB) pension schemes with assets of approximately £590bn and membership of 3.5m (around a third of the overall DB universe).

About GC100

GC100 is the association for the general counsel and company secretaries of companies in the UK FTSE 100. There are currently over 125 general counsel and company secretary members of the group, including representatives from over 85 of the UK FTSE 100 companies.

The aim of GC100 is to engage with government, regulators and policy makers to provide practical and business-focused input on law and regulation which impacts on the largest UK Listed Companies.

We are happy for the 100 Group and GC100 to be included on the list of respondents. Whilst this letter expresses the views of both the 100 Group of Finance Directors as a whole and GC100, these views are not necessarily those of our individual members or their respective employers.

We start with general comments and then go on to provide specific comments on the consultation questions which concern us most.

General Comments

In our comments, we have accepted what we understand to be the policy intention behind the draft regulations, being to provide the Pensions Regulator ("**Pensions Regulator**") with a revised notification 'early warning system' by which:

- the Pensions Regulator is told about corporate matters which could have a material impact on the employer covenant supporting a UK defined benefit pension scheme;
- it is told about these matters at a much earlier stage than it would normally be notified today so it can address any concerns it has while the matter is still being commercially negotiated; and
- the parties to a relevant matter understand that the Pensions Regulator has broad, material new powers (including criminal sanctions) which can be exercised in relation to the new Notifiable Events regime.

The 100 Group/GC100 appreciates the need for the Pensions Regulator to be able to identify matters which could have a materially detrimental effect on the employer covenant of a defined benefit scheme. However, its members are also keen to stress that the matters which need to be notified should be:

- *Certain* – companies need to understand what they need to do to comply and when; and
- *Targeted*: notification should only be required when it truly matters to protect against a material risk to an employer covenant, and so not place an inappropriate compliance burden on companies and the Pensions Regulator.

We would also like to stress the impact of the new criminal sanctions on the way that companies are likely to view the notifiable events regime. Notifiable events will be truly important from a risk management perspective, and so companies can be expected to:

(a) behave conservatively given the risks involved, and notify as much as possible to manage their risk, and

(b) want to understand the Pensions Regulator's reaction to an event being notified before proceeding with the corporate matter.

In relation to companies acting conservatively with many notifications, there is surely risk to the Pensions Regulator that it will receive so many notifications that it receives one that is material, misses its importance, and then there is some scheme abandonment (or similar). We suggest that fewer, more focused notifications would better serve the policy intent here.

In relation to companies wanting to know the Pensions Regulator's reaction, it is possible that deals may be subject to a condition precedent that the matter cannot close unless there is confirmation that no further action is to be taken by the Pensions Regulator following a notification being given. Has thought been given to how companies will be able to get the kind of 'sign off' that they are likely to want (given the risk of criminal sanctions)?

In terms of the definitions used and phrasing in the consultation, they appear to assume that applicable corporate events (transactions/re-financings etc) are linear: they have a beginning, a middle and an end. This however is very commonly not the case – they can be much more iterative and complex than this. In this light, we suggest that you may like to work through with us how the definitions work in practice with normal corporate activity.

We have various examples that our members have given us of corporate events which do not appear to fit the current structure well. Please let us know if it would be useful for us to meet with appropriate DWP representatives at your convenience to talk through these examples and try to understand how the new regime could work in practice.

Please also note that the existing employer-related event of 'relinquishing control of a DB scheme sponsor' is not always notifiable. Directions issued by the Pensions Regulator, helpfully, confirm that a report is not required where the scheme was at least 100% funded on the section 179 basis at the latest valuation and there has been no requirement for the trustees to report a failure of the employer

to pay contributions under the schedule of contributions. It would be helpful for the Government to confirm that this exemption will remain, in which case it would be helpful to also extend this to the two new notifiable events. In the absence of any indication to the contrary, it appears to us that the rationale for the Pensions Regulator's Directions would be equally applicable here.

Furthermore, we question whether it is necessary to persist with the trustee event of reporting high transfers (ie the lower of £1,500,000 or 5% of scheme assets). It is not clear to us whether the Pensions Regulator has ever initiated a Regulatory Intervention that has been of benefit to members based upon the information in these reports, in which case perhaps it could be removed altogether. If the Pensions Regulator considers that the reports remain a useful regulatory tool, we suggest that the wording of the regulations be amended so that only transfers that exceed the higher of the two thresholds need be reported – i.e. where the transfer is greater than the higher of £1,500,000 and 5% of assets.

Finally, we consider it important for the new Notifiable Events regime to fit with both the Takeover Code and the FCA Inside Information requirements, which both apply to our members. It is not currently clear that they have been taken into account in the Consultation.

Question 1: do you think that the definitions capture the policy intention? If not, please explain why.

We do not consider that the proposed definition of "decision in principle" captures the policy intention (as we set it out above in the General section).

The problem with the definition of "decision in principle" is that it assumes that an employer will first decide 'in principle' to go ahead with an event, and then negotiate its terms. This is not however how much relevant corporate activity occurs in practice.

Instead, the key negotiations tend to happen first before any 'decision in principle' is taken – as the terms on which a matter could be transacted are fundamental to whether a corporate board will wish to decide to do it (even in principle).

This means that a "decision in principle" may not be made until late in the negotiation process, possibly only a very few days before the transaction is signed.

Companies may however be advised that the intention behind the "decision in principle" concept is for the Pensions Regulator to be notified much earlier; at the start of negotiations before any decisions have actually been taken. If this happens, the Pensions Regulator will receive many notifications about possible future corporate events, many of which will never in fact occur and which the company has not decided to implement.

This would cause a material compliance burden for UK companies, and mean that the cost of complying with these Regulations far exceeds the costs described in the Impact Assessment at the end of the Consultation.

In terms of how best to address this (and acknowledging that the rules will apply to both listed and unlisted companies), you may find it useful for the "decision in principle" to marry up with the existing triggers for disclosure under Market Abuse Regulation for listed companies. Broadly, the market needs to be informed when a decision is sufficiently material that it would be expected to move the share price: this includes the decision being sufficiently progressed such that the disclosure is actually informative, and the market is not moved by 'red herrings' and false starts. This could help you to make the notifications targeted - as we describe above.

There could also be merit in the new notifiable event being in line with Class 1 transactions (requiring a shareholder vote) – i.e. about what to disclose.

Leveraging these existing concepts, rather than inventing new ones, could make the new law easier to apply. You would start with an existing body of expertise about when the right time to disclose is, rather than the Pensions Regulator being swamped with prudent but inappropriately early disclosures as people 'find their feet' on a new test. There is otherwise a real risk of obligations being imposed by the new regulations, which then need to be relieved by Pensions Regulator guidance as it tries to reduce the flow of notifications about immaterial events.

Another concern is how this regime fits with the insider information regime. The consultation is silent on this. Assuming it is the policy intent that the Pensions Regulator should receive notifications at a very early stage of a corporate matter, it will need to give individual names of Pensions Regulator employees to come onto insider lists. (Trustees will similarly need to come onto insider lists when the 'accompanying statement' is given.)

It is worth the Pensions Regulator being comfortable with the practical consequences of this. The Takeover Panel is obviously very familiar with how this works: we suggest that the DWP may wish to discuss the consultation with the Takeover Panel and include details in its response to the consultation on how the new regime works with the inside information rules etc.

Question 2: can you see any unintended consequences of these amendments?

We have concerns about the meaning of "offer".

Our members are listed companies. The Takeover Code already requires the trustees of defined benefit pension schemes to be notified at set times in the takeover process. It would be helpful for the Regulations to address the relationship between these requirements and the notification to be made on receipt of an 'offer'. It is not clear at present.

In addition, a notification would be required once any offer has been made, no matter how immaterial or uncommercial (for example, multiple £1 offers from a pressure group looking to cause issues for a company). This again means that notifications could be necessary on receipt of offers which have no impact on the employer covenant of the defined benefit scheme. It would be useful if a materiality threshold could be added to this notification requirement, or perhaps link notification to where the offer was sufficiently material for it to be considered by the Board of the target company (or of its parent).

Question 3: are there any unintended consequences of this approach? What is the impact on multi-employer schemes and the employers? Is there a simple way of apportioning liabilities which would work for all multi-employer schemes?

There are unintended consequences with the proposed revised approach, which could have material consequences for multi-employer schemes and their employers.

We believe the key point here goes back to the need for "targeted" notifications as described in the General section above. As proposed, the sale of 25% of the business or assets of a small, or immaterial employer will have no material impact on the employer covenant, but would need to be notified (potentially multiple times under the new regime). This appears to be disproportionate.

We suggest that the key is to focus on what could have a material impact on the employer covenant. So, in a multi-employer scheme, there are normally one or two employers whose covenant is truly material. Could the trustees be asked to identify these, and these then be tracked for the 25% test?

An alternative would be to apply the 25% test on a group-wide basis using numbers in consolidated accounts.

Question 4: do you agree that "when the main terms have been proposed" is an appropriate point for the notice and statement to be issued? Can you see any unintended consequences of using this definition? At what point would it be reasonable for employers to have discussions with the trustees about the intended transaction?

We do not consider that "when the main terms have been proposed" is an appropriate point for the notice and statement to be issued. As noted above for the "decision in principle", main terms can be proposed very early in a possible transaction before any negotiations and any decision has been taken – even in principle.

For example, on a refinancing, businesses commonly get a quote from a lender which sets out most of the terms including potentially a request for security. The business will often get several of these, and not act on most, or sometimes any, of them.

There is also a question about when it is appropriate to bring pension trustees in on a proposed transaction. Given what we say above, there is a real risk that pension trustees are brought into a

proposed transaction very early (being when "main terms have been proposed"), when in reality the matter may not proceed and the possible impact on the pension scheme is far from clear.

We suggest it would be better to identify a time when there is sufficient information about the relevant matter for the employer and the trustees to understand (and agree mitigation for) any effect on covenant.

Question 5: Does the definition of relevant security meet the intention that it will apply to granting of security which may affect the employer's ability to support the scheme? Are there any unintended consequences? Should other specific types of security be included or excluded? Is it appropriate to specify a 25 per cent threshold by reference to revenues or assets as proposed?

First, we welcome the proposal to exclude a refinancing of existing debt from the notification. This is important for our members.

We assume that the reference to what is included in the definition of 'relevant security' is a non-exhaustive list? Fixed and floating charges are good clear terms but could other things be included? It is important to have certainty here. For example, in a commercial loan document with a negative pledge clause, there are likely to be exclusions from the negative pledge which are permitted security interests. This list of allowable security interests may have 20 sub-clauses, each of which potentially needs to be checked to see if it could be a 'relevant security'. This may not however be clear.

Similarly, we have businesses that must provide assurance to local regulators over decommissioning liabilities which could be outside of the UK. This is common in the nuclear industry as well as extractive industries such as the oil and gas sector. The financial assurance can involve cash and investments being placed in ring-fenced entities secured in favour of regulators. The amount can change frequently, by additional contribution or investment returns. It is not clear in scenarios such as this, whether notification to the Pensions Regulator will be required if the relevant 25% threshold is passed.

Another example of security that is granted in the normal course of business is repurchase agreements (repos). Here businesses receive security over a pool of financial assets posted to an agent by the bank counterparty. Businesses can determine the quality of the financial assets – for example by reference to credit rating or issuer. At the end of the investment term, the cash is repaid and security over the assets is released. This is a common corporate treasury investment approach and provides enhanced financial strength for the investor and helps the bank reduce its balance sheet. The alternative is investing a lower return directly with the bank, and taking on exposure to the bank's credit risk. It is not clear whether changes to the receipt of repos security would be notifiable, again if the 25% threshold is crossed.

Finally, we would also highlight security given as part of project finance arrangements. Our members include large companies who would commonly partner with a third party on a large project and form a joint venture which is bank-financed. Banks often ask for a charge over the company's shares in the joint venture company, as well as guarantees. These arrangements could be caught in the definition of 'security' and so materially impact the normal activities of these companies.

Question 6: do you agree this is a reasonable definition of revenue and assets? If, not, how do you consider they should be defined?

We have one concern about the meaning of 'assets'. As there is no materiality threshold for the size of employer in the draft Regulations, many employers could turn over more than 25% of their total asset value in sales of stock in a 12-month period. We assume that this is not the policy intention.

We suggest that this could be addressed by focusing not on sales but rather on the value of the assets which makes up the employer covenant supporting the scheme.

Question 7: do you consider that 25 per cent of the revenue or assets is an appropriate level? If not, please indicate what you think is an appropriate level and why?

No comments

Question 8: do you agree that disposals which have taken place or agreed within 12 months of the date of the notifiable event should be taken into account when calculating the 25 per cent threshold? If not, please explain why.

We understand the reasons for the approach that has been taken here (which we assume to be an anti-avoidance measure). However, on the basis of the current Regulations, once the 25 per cent threshold has been passed, every subsequent transaction in the next 12 months will need to be notified (even if very small, and even where the Pensions Regulator has already examined those transactions and any mitigation has been agreed).

Is there instead a way that, if transactions in a 12-month period have been reviewed and 'signed off' by the Pensions Regulator already, any new transactions in that 12-month period would only need to be notified if they cross a new 25% threshold?

Please see our comments above about the importance of the Pensions Regulator giving companies a 'sign-off' on a transaction that has been notified.

Question 9 (contents of accompanying statement): does this list provide all the information which should be notified to The Pensions Regulator? If not, what else should be included?

No comments

Question 10 (meaning of material change): Do you think this meets the policy intention or are there any unintended consequences?

We are concerned that, given how early notifications may need to be made when negotiating a transaction, there will be multiple 'material changes', each of which will need to be notified. Each of these is unlikely to be material in terms of the effect of the 'material change' on the employer covenant available to the DB scheme.

This accordingly goes back to the principles described in the General section above: it would be good in relation to all the proposals in the Consultation to ensure that notifications are only going to be needed where they relate to something that has a material impact on employer covenant. There is otherwise a real risk that multiple notifications will be needed for many types of corporate event.

We hope that you find these comments useful. Please do not hesitate to contact us if you would like to discuss any of the points raised. We would in particular be happy to meet to discuss collaboratively the practical application of the Regulations and any changes to help them to be more certain and targeted in addressing your policy intentions.

Yours faithfully,

Phil Aspin
Chairman
The 100 Group Pensions Committee

Camelia Thomas
Secretary
GC100