



# Pensions: when should employers disclose a proposed transaction?

EMPLOYMENT, PENSIONS AND BENEFITS BRIEFING 188

An employer may have good reasons to delay notifying the trustees of a defined-benefit scheme, the Pensions Regulator or scheme members about a proposed transaction – especially if the transaction is not yet finalised. But failure to notify may be a breach of the employer's legal obligations and can have significant consequences.

This briefing explains the legal obligations to notify these parties and when these may be triggered.

An employer may, for example, be reluctant to share information if it is concerned that involving more parties in negotiations will complicate, delay or frustrate a proposed transaction.

However, sharing information with a pension scheme's trustees may help build and maintain a co-operative relationship with them – something that can be crucial in scheme funding negotiations or if the employer envisages asking the Pensions Regulator (the Regulator) to provide clearance for the transaction.

Furthermore, an employer is sometimes legally obliged to disclose information about a proposed transaction to the pension scheme trustees, the Regulator or pension scheme members. These obligations are often triggered before the transaction is finalised and breaching them can, among other things, lead to the Regulator imposing civil penalties on the employer and its directors.

## Do you have to disclose information to the trustees?

### Are you contractually obliged to disclose the proposed transaction?

An employer may have to inform the trustees about a proposed transaction if it has, or other companies in its corporate group have, entered into a legally enforceable agreement with the trustees to notify them of its corporate activity.

## Is there a statutory duty to disclose the proposed transaction?

The Occupational Pension Schemes (Scheme Administration) Regulations 1996 (the Scheme Administration Regulations) require employers:

- on the trustees' request, to disclose information to the trustees or managers that is reasonably required for the performance of their duties or their professional advisers' functions – regulation 6(1)(a); and
- to disclose automatically to the trustees or manager the occurrence of any 'event' relating to the employer if there is reasonable cause to believe that it will be of 'material significance' in the exercise of the trustees' functions or the functions of their professional advisers – regulation 6(1)(b).

If the obligation to disclose information is triggered under regulation 6(1)(b), the employer must make the disclosure within one month of the event's occurrence.

It will not always be clear at what stage during a transaction (which is of material significance) the obligation to disclose an event will be triggered. This is because the regulations do not elaborate on what is meant by an 'event'.

In the Regulator's view an 'event' includes 'events which result in a corporate transaction or any event which impacts on the benefits of scheme beneficiaries'.<sup>1</sup> On this interpretation, an employer should consider disclosing

<sup>1</sup> Paragraph 86 of the Pension Regulator's guidance on conflicts of interest ([www.thepensionsregulator.gov.uk](http://www.thepensionsregulator.gov.uk)).

the occurrence of key steps that lead to the signing or completion of a corporate transaction, because the Regulator is taking the view that an employer may trigger this disclosure obligation before ultimate signing or completion. But, in practice, it may be difficult to apply the Regulator's interpretation because the employer may not know (at that time) if negotiations, for example, will in the future 'result' in a transaction completing. The transaction may still not complete.

Breach of either the 'on request' or automatic disclosure requirements can lead to the Regulator imposing a maximum civil penalty of £5,000 for individuals and £50,000 for companies. This penalty can extend to the employer's directors or officers who consented to the breach.

#### **What if there is a conflict between duties owed to the employer and duties owed to the trustees?**

An employee or officer (eg the financial director) of the participating employer who has a dual role as a pension scheme trustee may face a difficult decision over whether to disclose information about the proposed transaction to the other trustees. This difficulty arises because a trustee may owe an implied duty to disclose material information to the other trustees. If such a duty exists (and the case law is unclear), this may conflict with an opposing duty of confidentiality owed to the employer.

Unfortunately the law is unclear on how a trustee's duty of confidentiality can be reconciled with a conflicting duty of disclosure. But any conflict needs to be effectively managed because there is a real risk of breaching one of these duties. Breach may result in sanctions – for instance, if the Regulator becomes aware of the conflict it could seek to impeach or sanction the trustee, using its powers to remove or replace trustees and announce this publicly.

There are a number of strategies that can be used to manage this conflict and avoid making a disclosure. For example, the trustee can exclude himself from the trustee board's decision-making process. However, the Regulator may not believe this will necessarily excuse a trustee from a duty to share information – see our briefing 174 on [Conflicts of interest: the Pension Regulator's guidance](#).

Alternatively, a conflicted trustee may sometimes be able to share confidential information with the other trustees without breaching a duty of confidentiality that is owed to an employer – eg if the employer expressly consents to the disclosure or if the employer and trustees have entered into a confidentiality agreement that permits such disclosures.

However, given that there is a real risk of trustees breaching a fiduciary duty to the employer by disclosing such confidential information, the prudent course is not to disclose without first obtaining legal advice.

For more information see our client guide on [Should the finance director be a pension trustee?](#)

#### **Is it in your best interest to disclose the information to the trustees?**

The employer's directors may owe a duty to the employer to inform the scheme trustees about a proposed transaction at an early stage.

Under the Companies Act 2006 directors have a general duty to 'promote the success of the company'. In complying with this duty they are required to consider the likely long-term consequences of their decisions.

With this in mind, it may be in the employer's best interest to inform the trustees about a proposed transaction if there is a significant risk that not informing them may lead to them taking actions that are potentially more detrimental to the employer than decisions they would otherwise have taken.

The risk of the trustees taking such adverse actions will vary and depend on the trustees' powers under legislation and the scheme's documentation (for example, they may be able to switch to a more conservative investment strategy). Trustees' ability to take such adverse action is further strengthened by their ability to call on the Regulator for assistance or by refusing to co-operate with a clearance application (see below).

#### **Are you expecting to ask the Regulator for clearance?**

If the employer envisages asking the Regulator for clearance, it is best to share information with trustees at an early stage.

Clearance is a voluntary process and provides reassurance that the Regulator will not, as a result of the transaction, use its moral hazard powers to make an employer or ‘connected’ or ‘associated’ third party liable for the pension scheme deficit (for more information see our briefing 178 on [Who is ‘connected’ or ‘associated’?](#)). The trustees’ support for a proposed transaction can be crucial in getting clearance from the Regulator.

Furthermore, the Regulator in its 2008 clearance statement says that it ‘expects trustees to, as soon as reasonable, be involved in any application... [and] For an application to proceed efficiently, the regulator will expect trustees to have had the opportunity to efficiently assess the impact of a type A event, to consider appropriate mitigation, negotiate where appropriate and take independent advice where needed.’<sup>2</sup>

Clearance will usually be appropriate only if the transaction is ‘materially detrimental to the ability of the scheme to meet its pensions liabilities’ (this is called a ‘Type A event’) – for example, if the transaction weakens the employer’s covenant to such a degree that it could be considered materially detrimental to the scheme’s ability to meet its liabilities.

### **Confidentiality agreement?**

It is worth considering putting an express confidentiality agreement in place if information is shared with the trustees. Information provided also needs to be accurate and not misleading.

## **Do you have to disclose a proposed transaction to the Regulator?**

### **Is the transaction a ‘notifiable event’?**

The Pensions Regulator (Notifiable Events) Regulations 2005 (the Notifiable Events Regulations) require employers to notify the Regulator of proposed transactions that involve ‘employer related events’ (for more information see our briefing 180 on [The Pensions Act 2004: obligation to report certain events to the Pensions Regulator](#)).

<sup>2</sup> Paragraph 96 of the clearance guidance ([www.thepensionsregulator.gov.uk](http://www.thepensionsregulator.gov.uk)).

Employers must always notify the Regulator of the following events:

- any decision by the employer to take action (eg to compromise a debt under section 75 of the Pensions Act 1995) that will, or is intended to, result in a debt that is (or may become) due to the pension scheme not being paid in full;
- a decision by the employer to cease to carry on business in the UK or cessation of business in the UK without such a decision being made;
- receipt of information by the employer that it is trading wrongfully within the meaning of section 214 of the Insolvency Act 1986 or if the director or former director knows that there is no reasonable prospect of avoiding insolvent liquidation; and
- a conviction, in any jurisdiction, of an individual for an offence involving dishonesty while they were a director or partner of the employer.

For some notifiable events, employers are not required to notify the Regulator if the scheme is fully funded (on a Pension Protection Fund basis) and the trustees or managers have not been required (in the past 12 months) to report to the Regulator a materially significant failure to pay contributions to the scheme. Otherwise, an employer will have to notify the Regulator if any of the following occurs:

- the employer breaches a banking covenant (unless the bank agrees not to enforce the covenant);<sup>3</sup> or
- a decision by the controlling company to relinquish control of an employer company or, if such a decision was not taken, the relinquishing of control.

It is important to note that some of these events can trigger a notification obligation at the decision-making stage, which can be before a transaction is completed.

The Regulator must be notified as soon as reasonably practicable after the person making the notification becomes aware of the notifiable event (for some events this must be before the actual action – eg a decision to make a transfer payment must be notified before the transfer is made). The Regulator’s guidance indicates

<sup>3</sup> The Regulator has told us that if the notifiable event is a breach of a banking covenant, it expects the employer to notify it within the required timescales even if the bank later grants a retrospective waiver of the breach.

that this obligation implies urgency: 'For example, where a trustee is made aware of a notifiable event on a Sunday, the Regulator should be notified on Monday.'<sup>4</sup>

The Regulator can impose a civil fine on an employer (and the directors and officers who cause a company to fail to comply with its obligations) if it fails to comply with the notifiable obligation without reasonable excuse. The maximum civil fine is £5,000 in the case of individuals and £50,000 in the case of a company.

The Pensions Act 2004 also stipulates that failure to notify a notifiable event may, in some circumstances, make it 'reasonable' for the Regulator to issue a contribution notice under its moral hazard powers.

### What if you're applying for clearance?

Employers need to share information about a proposed transaction with the Regulator if seeking clearance for a transaction (see above).

Before formally applying for clearance, parties can contact the Regulator on a no-names basis to enable subsequent discussion between trustees and employers to take place with a high-level understanding of the Regulator's views. At this stage, the Regulator would probably have to be informed about the nature of the proposed transaction. However, specifics about the transactions or the parties to the transaction will not yet need to be divulged.

If making a formal clearance application, parties will then need to provide a full and accurate disclosure of the circumstances surrounding the proposed transaction. Failure to provide full and accurate information may render clearance worthless because the Regulator can set it aside if the circumstances described in the application are not the same as those arising and this is material – see sections 42(5) and 46(5) of the Pensions Act 2004.

### Confidentiality agreement?

Employers will probably not need to enter into a confidentiality agreement with the Regulator when informing it. This is because the Regulator is subject to express confidentiality obligations (but there are some exceptions, such as disclosure to other government departments). The Regulator, usually, cannot (for example) disclose the information to the trustees, unless the employer has consented to such disclosure.

## Do you have to inform your pension scheme members about a proposed transaction?

Sections 259 to 261 of the Pensions Act 2004 require employers to consult affected scheme members if the employer (or another person, such as another company with the group) is proposing to make a 'listed change' to the pension arrangement. The obligation applies to employers that have over 50 employees (not scheme members).

If an employer is proposing to make a listed change, it must inform affected scheme members (and their representatives) at least 60 days before any decision is made and then consult.

A listed change includes preventing 'the future accrual of benefits under the scheme for or in respect of members or members of a particular description' and it is arguable that this can apply in relatively common transactions if a company stops participating in a group pension scheme following a sale of the company out of the group or there is a transfer of its business under the Transfer of Undertakings (Protection of Employment) Regulations 2006 (commonly referred to as the Tupe Regulations).

The argument is that such transactions may entail a listed change because cessation of participation will mean the end of future accrual of benefits under the seller's scheme. But there are strong contrary arguments – the point needs to be considered taking into account the specific circumstances.

The Regulator has the power to impose a civil penalty if an employer has, without reasonable excuse, failed to comply with its consultation obligations. The maximum civil penalty is £50,000 (£5,000 for an individual).

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<sup>4</sup> Paragraph 16 of the Regulator's Code of Practice on notifiable events ([www.thepensionsregulator.gov.uk](http://www.thepensionsregulator.gov.uk)).