EVERSHEDS SUTHERLAND

Flagging the issues
How Brexit will impact the future of pensions

On 23 June 2016, the UK held a referendum on its membership of the European Union (EU), with a majority voting in favour of the UK leaving the EU. Although the UK is currently scheduled to leave the EU on 29 March 2019, remember, *'nothing is agreed until everything is agreed'!* However, assuming the UK does leave the EU, the uncertainty of Brexit won't end on this date.

Once the UK has left the EU, the next stage will be for Government and Parliament to review and decide which EU-derived law to retain, amend or revoke, using the powers contained in the European Union (Withdrawal) Act 2018. The nature and content of any final withdrawal agreement with the EU (which is currently unknown) will determine the amount of EU-derived law retained in the long term; in the event of a "no deal" exit, regulations already laid before Parliament under the provisions of the 2018 Act will make detailed amendments to domestic pensions legislation reflecting the ending of the UK's membership of the EU – for instance, the ending of the special regulatory treatment for cross-border pension schemes. This note assumes that the UK will leave the EU (which is the default position unless the 2018 Act is repealed or amended), but this remains uncertain given the fractious nature of the ongoing Brexit debate.

What are the implications?

In the short term, Brexit is unlikely to have a significant impact on the legal and regulatory framework for UK pension plans (other than cross-border schemes). However, it does open the door for UK legislation to deviate from EU requirements in the future (for example, in relation to funding, investment and plan governance). Furthermore, without the influence of the CJEU in the background, UK case law on matters previously the preserve of the EU, such as equal treatment and TUPE, may start to take its own domestic direction.

Any political fallout following Brexit could have a major impact on the future shape and direction of UK pensions policy. However, it is fairly likely that the UK, whatever the colour of politics, will probably choose to formally distance itself from certain EU originated policies which have never fitted very well with the UK pensions system (for example, age discrimination laws and the reclamation of VAT on investment costs).

In the more immediate future, there is likely to be considerable investment volatility, which could present both risks and opportunities for pension plan trustees and corporate sponsors. The position will need to be monitored carefully, and trustees in particular will need to consider quickly whether their plan's investment portfolio remains appropriate for a post-Brexit world. Plan investments governed by the laws of another member state or contingent assets based in the EU will need particularly close attention to ensure they remain appropriate and enforceable.

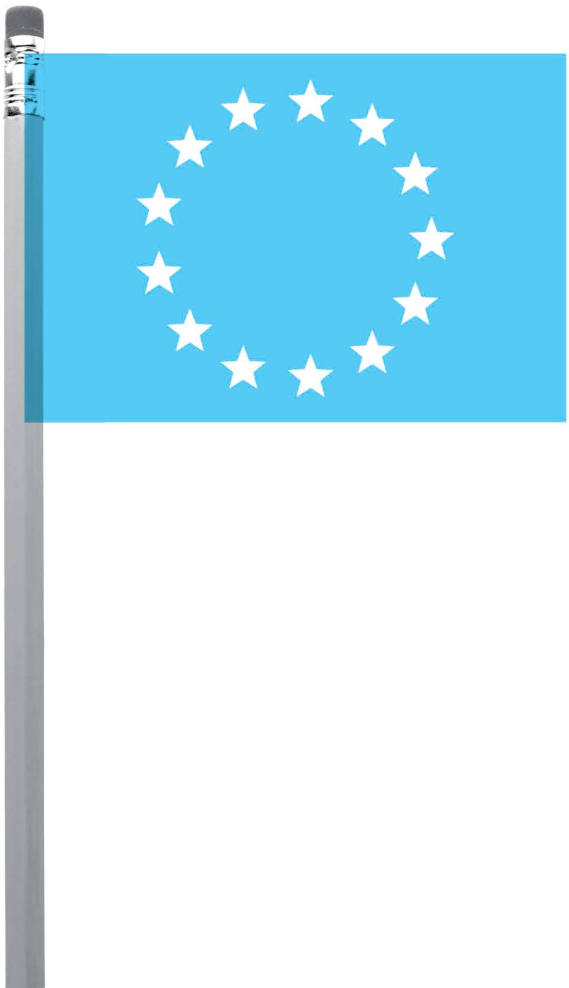
The macro-economic impact of Brexit and its impact on individual businesses is difficult to predict with certainty as it is likely to be determined, to a large extent, by the nature of the UK's ongoing relationship with the EU as well as any trade deals that the UK enters into with countries outside of the EU (such as the US and China). Trustees of defined benefit pension plans need to be alive to any deterioration in the financial strength of the business standing behind their plan and corporate sponsors need to be prepared to address trustees' concerns in this regard. The impact of a "no deal" exit in particular is difficult to predict with any degree of certainty, and trustees with sponsors whose businesses are particularly vulnerable to the kinds of disruption forecast in a "no deal" scenario may need to scrutinise the details of their sponsor's contingency planning with additional care.

On 24 January 2019, the Pensions Regulator (TPR) issued a short **statement** which was aimed primarily at trustees of DB schemes and reminded trustees and sponsors of their 2016 statement. TPR does not expect the UK's withdrawal from the EU to have a significant impact on the legislative framework applying to schemes or on trustees' ability to administer their schemes effectively as UK pension schemes are largely domestic in nature; but it is notable that the new TPR statement emphasises the need for trustees to consider contingency planning in respect of a "no deal" exit, in particular where the scheme is an authorised cross-border arrangement.

The Pensions and Lifetime Savings Association has produced a **Brexit-to-do-list** for trustees. This sets out 10 steps to ensure their pension plan can deal with Brexit, including reviewing the employer covenant funding status and investment strategy (as also referred to in the table below).

The post-Brexit legal landscape for pensions will depend upon the following that have yet to be determined:

- the terms of the UK's exit of the EU
- the UK legislature's approach towards areas derived from EU law
- the terms of any memberships and free trade agreements



The immediate concerns

The following table sets out some practical matters that employers and trustees should be considering now, particularly as exit day approaches:

Area	Description	Action
European judgments	Subject to any implementation period, courts in the UK will no longer be obliged to follow post-Brexit rulings of the CJEU, nor will there be any right to refer questions of law to the CJEU. In the same way that legislation originating from EU law will remain on our statute books, historic CJEU case law will be given the same binding, or precedent, status in the UK courts as decisions of the supreme court. Any post-Brexit CJEU judgments, the UK courts may continue to refer to such judgments to guide their interpretation of that legislation. However, they will be of persuasive authority only.	No immediate action required.
Legislation	In the immediate aftermath of Brexit, no significant changes are expected in relation to legislation affecting pension schemes. Data transfers from the EU to the UK should be permitted through the Data Protection Act 2018 following GDPR (although the government could make amendments to that framework post-Brexit if it wanted to). The UK is committed to implementing the requirements of the IORP II (or Pensions) Directive which contains new requirements on plan governance and member communications.	No immediate action required.
State pensions	EU-wide legislation currently co-ordinates UK social security schemes which may cease to apply on Brexit. The possibility of EU-wide developments and bilateral agreements will need to be monitored to see how individuals will be affected in the longer term.	No immediate action required.
Sponsor covenant	Many different elements will impact on changes to any given sponsor's covenant, such as a reliance on cross-border suppliers or customers, tariffs affecting price and ease of movement, any impact on currencies and changes to group operations.	Corporate sponsors should be assessing the potential impact of Brexit on their business and their pension plan to prepare contingency plans. Trustees should continue to assess/monitor the covenant backing their pension plan.
Counterparties and enforceability	The impact of the enforceability of arrangements and commitments trustees have with investment or other counterparties, sponsors or guarantors that are EU entities should be considered to ensure they remain appropriate and enforceable.	
Investment implications	A failure of investment managers to respond appropriately or undertake any mitigating actions for any outcome of Brexit risks a temporary failure of supply chains.	Trustees should ask investment managers if plans are robust and comprehensive enough for Brexit to ensure there are no operational implications for investments.
De-risking	De-risking the investment strategy could reduce the uncertainty and risks posed throughout Brexit and its immediate aftermath. Market conditions could mean attractively priced opportunities for DB pension plans to enter into buy-in or buy-out deals, depending on their investment mix and assuming they can move quickly.	Trustees should consider the suitability of their post-Brexit portfolio and what steps they can take to mitigate the impact of continued volatility on investment markets on their pension plan.
Member communications	Trustees and corporate sponsors should consider the need to send a communication to plan members to reassure them about the steps that they are taking to mitigate any risks to the plan arising as a result of Brexit.	This should be ongoing.
Cross-border pensions	Brexit, assuming it involves leaving the EEA as well as the EU and subject to any implication period, will mean that the cross-border rules will no longer apply to UK schemes.	This should be assessed as soon as the terms of Brexit are determined. TPR has indicated that cross-border schemes will need to be considering contingency plans in particular for a "no deal" exit.

Contact

Charmian Johnson
Partner

T: +44 161 831 8187
M: +44 782 552 2461
charmianjohnson@
eversheds-sutherland.com

@ESpensionlaw

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