

news

PPF Entry and apportioning DB liabilities

Will the apportionment of liability between participating employers in a defined benefit (DB) occupational pension scheme cut off possible future access to the Pension Protection Fund (PPF)? This is the question posed in the recent case of *L & Others v M Ltd (L v M)*. The judgment sheds light on the rarely litigated (but highly complex) section 75 of the Pensions Act 1995¹ and the equally convoluted regulations governing entry to the PPF.

Background to the *L v M* case

The Pension Proposal

- The Company was the sole participating employer in a DB scheme (the Scheme) whose funding shortfall was approximately £9.5 million under FRS 17 and around £38 million on a buy-out basis.
- Having run at a loss for some years, a restructuring plan was devised to prevent the Company going into insolvency.
- This involved, amongst other things, the “Pension Proposal”.

The Pension Proposal

In summary

- A new company (Newco) is established and starts participating in the Scheme.
- The Scheme rules are amended to apportion any liability under section 75 so that £1 is payable by the Company and the balance by Newco.
- The Scheme winds up and, having paid its £1 section 75 debt, the Company ceases to be an employer for PPF purposes.
- Newco is unable to meet the balance of the estimated £38 million buy-out debt and suffers an insolvency event.
- The Scheme is tipped into the PPF².

The Law

Section 75 and multi-employer schemes

- The scheme actuary is responsible for calculating the difference between assets and liabilities in a scheme under section 75.
- In multi-employer schemes, the scheme rules can set out how this difference is then apportioned between participating employers.
- Otherwise, a statutory default calculation applies.

¹ Section 75 regulates the debts payable by employers to underfunded DB schemes on the occurrence of certain triggering events including scheme wind-up, employer insolvency and an employer leaving an ongoing multi-employer scheme

² In return, the PPF Board takes an (undisclosed) equity stake in the restructured business

The Law

The PPF Entry Regulations

- These regulations generally prevent section 75 debts being compromised and the PPF being saddled with responsibility for underfunded DB schemes.
- Specifically, regulation 2(2) prevents schemes from entering the PPF where at any time trustees “*enter into a legally enforceable agreement the effect of which is to reduce the amount of any debt due*” under section 75.
- So what did this mean for the Pension Proposal and the proposed apportionment rule to be inserted into the Scheme rules?

A tale of two constructions

The “broad view”

The “narrow view”

- The case essentially hinged on two different interpretations of when regulation 2(2) applies (thereby precluding access to the PPF).
- The “*broad view*” (deliberately argued on behalf of the trustees to test PPF entry) is that regulation 2(2) bites on a wide range of agreements, even those which compromise contingent debts which may (or may not) become payable in the future.
- The “*narrow, narrow view*” restricts regulation 2(2) to agreements made only where a section 75 debt has been both triggered and calculated by the actuary.

The judgment

- Mr Justice Warren decided upon a narrow construction of regulation 2(2), allowing the Pension Proposal to go ahead without risking PPF eligibility.
- But, in many ways, the *L v M* decision is limited to its very specific facts.

The wider implications

- Helpfully, the case offers insights into the use of section 75 apportionment rules and their drafting (although how they square with the Regulator’s anti-avoidance powers is still open to some debate).
- Somewhat confusingly, the judge offers a third meaning of regulation 2(2) which catches any legally binding compromise agreement entered into after section 75 has been triggered but **before** the debt has been calculated (the “*broad, narrow view*”).
- This would pose problems for trustees exercising a discretion to apportion where an employer exits an ongoing multi-employer scheme.
- Further judicial clarification is therefore desperately needed.

SACKER^S
& PARTNERS

Solicitors specialising in pensions law

Sacker & Partners LLP
29 Ludgate Hill
London EC4M 7NX
Tel 020 7329 6699
Fax 020 7248 0552

enquiries@sackers.com
www.sackers.com

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