NOVEMBER 2004

news

sackers extra

pensions reform 2004-05

Anti-avoidance – a "moral hazard"?

The so-called "moral hazard" provisions in the Pensions Bill have stolen many column inches since they were first announced in April 2004. Broadly, their effect is to widen the scope of parties who may be made responsible for a pension scheme deficit. The importance of this is heightened by the fact that, in future, the level of debt due will be full buy-out in all circumstances.

Moral Hazard

The rationale

- Commenting back in April 2004, the Pensions Minister, Malcolm Wicks, said:

  "The new clauses should act as a deterrent to employers who are considering dodging their pension obligations. They will also provide reassurance to responsible employers that their levy payments will not be subsidising unscrupulous employers…Mitigating the risks of moral hazard is one of the biggest challenges we face in introducing the Pension Protection Fund."

Moral Hazard

A summary

- The moral hazard provisions build on and extend the scope of the existing debt on the employer provisions in section 75 of the Pensions Act 1995.
- The Pensions Regulator has three key powers – Contribution Notices, Financial Support Directions and Restoration Orders.

Contribution Notices (CNs)

Catching debt avoidance

- The Regulator may issue CNs if it believes there has been an act or a deliberate failure to act (since 11 June 2003) which reduces a section 75 debt, or which prevents it becoming due or being paid.
- CNs can be issued against an employer (or those connected or associated with it) or anyone who knowingly assists.
- CNs are not limited geographically, save that debt enforcement may be easier to procure in some countries than in others.

Financial Support Directions (FSDs)

Scheme participation unnecessary

- FSDs can be issued where a scheme employer is a "service company" or is "insufficiently resourced…to meet... a prescribed percentage of the estimated section 75 debt".
- They can be aimed at group employers even if they do not participate in the scheme, and will effectively require the recipient to take responsibility for pension scheme liabilities.
- If a person fails to meet an FSD, a CN can be issued.

Restoration Orders (ROs)

Transactions at an undervalue

- ROs may be made where, on or after 11 June 2003 and within two years of an employer's insolvency, there has been a transaction at an undervalue (TUV) involving scheme assets.
- For example, a TUV could conceivably include the payment of an enhanced transfer value just before an insolvency event.
- Again, a CN can be issued if an RO is not met.

Recent changes

Responding to corporate concerns

Following criticism, the Government recently put forward changes which seek to tone down the moral hazard clauses. These include:

- excluding Insolvency Practitioners from the ambit of CNs and other "prescribed" persons;
- imposing a six year time limit for issuing a CN;
- possibly bringing factors such as saving jobs into the equation when deciding whether to impose liability under a CN;
- introducing a clearance procedure to allow the Regulator to bless acts etc. which might otherwise be caught by either a CN or FSD.

Conclusions

Tread carefully

- The implications of the moral hazard provisions are potentially extremely far-reaching.
- Much will depend on the approach the Regulator adopts.
- But these new powers will no doubt continue to take centre stage in corporate transactions and restructurings.

This edition of Sackers Extra News is part of a series focusing specifically on pensions reform. Our Pensions Reform Team will continue to keep you abreast of the key issues throughout this period of pensions simplification.
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