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Pensions Bill catch-up

1 BACKGROUND

On 18 October 2004, a new version of the Pensions Bill was printed. The new version catches up on all of the changes made to the Bill since 21 May 2004, when the Bill left the House of Commons to be considered by the House of Lords. Given this time-lag, many of the new clauses featured in the Bill have already received a certain amount of publicity.

However, with less than a month to go before the Bill is scheduled to receive Royal Assent, we set out below a brief summary of some of the more significant additions.

2 WINDING-UP PRIORITY ORDER

Under a key new clause, a new priority order on the winding-up of a defined benefit pension scheme will be introduced. It is likely that the new order will affect schemes which begin winding-up on or after 6 April 2005. The new order is intended to protect the Pension Protection Fund (PPF) by ensuring that the PPF level of benefits are a high priority for trustees when distributing available assets.

In summary, the new order will look as follows:

2.1 Relevant pre-6 April 1997 insurance contracts

The Government's focus here is on insurance contracts which cannot be surrendered or, if they can, the amount payable on surrender "does not exceed the liability secured by the contract";

2.2 Benefits which do not exceed the "corresponding PPF liability"

Because of the way in which the PPF works, members' benefits will need to be secured under this priority broadly as follows:

- 100% of pension for members who have reached the scheme pension age or who are receiving ill-health pensions;

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- 90% of benefits for everyone else (including a pensioner who has not reached the scheme pension age) subject to a pension cap (initially £25,000 per annum).

The PPF liability excludes pension increases attributable to pensionable service prior to April 1997 and caps increases from 6 April 1997 at 2.5% per annum (not 5%);

2.3 Voluntary contributions

Unless they are already covered under the priorities referred to in 2.1 or 2.2;

2.4 Remaining benefits

Any remaining benefits not mentioned under the above categories.

3 ANTI-AVOIDANCE MEASURES (MORAL HAZARD)

Designed to protect members and the PPF by deterring employers from walking away from pension scheme debts, the so-called "moral hazard" clauses have courted controversy since they were first announced in May 2004. To recap, the moral hazard clauses have three main strands:

3.1 Contribution notices

The Pensions Regulator may issue such notices if it believes that an act or "deliberate failure to act" on or after 11 June 2003 has resulted in an employer avoiding paying a statutory debt. Where the Pensions Regulator believes this has happened, those potentially in the firing line include anyone associated or connected with the employer, or those who "knowingly" assisted.

3.2 Financial support directions

Such a direction may be made if the Pensions Regulator considers, for example, that the sponsoring employer of a pension scheme is "insufficiently

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resourced" to meet a prescribed percentage of the estimated statutory debt. Other group employers (even if they do not participate in the pension scheme) can be called upon to stand behind the debt. The Pensions Regulator can issue a "contribution notice" if a financial support direction is not complied with.

3.3 Restoration orders

Restoration orders 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" involving scheme assets (for example, the payment of an excessive transfer value). Again, a contribution notice can be issued against anyone who fails to comply with an order.

To help alleviate concerns about the width of these clauses and their potential ramifications, the Government has put forward a number of changes. Although the new print of the Bill has not yet caught up with these latest proposals, they include:

- in general imposing a time limit of 6 years within which the Pensions Regulator must issue the contribution notice;
- where relevant, requiring the Pensions Regulator (when deciding "whether it is reasonable to impose liability") to take into account "all the purposes of the act or failure to act (including whether a purpose of the act or failure was to prevent or limit loss of employment)";
- introducing a clearance procedure under which an application can be made to the Pensions Regulator regarding a particular transaction which might otherwise be caught by either a contribution notice or a financial support direction;
- limiting the potential class of individuals who may be required to contribute financially under the moral hazard clauses.

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4 MISCELLANEOUS

Other clauses now in the Pensions Bill include:

- **Early leavers** – members who leave a scheme after more than three months' pensionable service, but without having reached the scheme's threshold for the provision of accrued benefits, will have new rights. Trustees will generally need to give such members the choice between a contribution refund or a cash transfer.

- **Member-nominated trustees/directors** – both active and pensioner members (or "an organisation which adequately represents" them) will now need to be involved in the nomination process. But the Bill is currently silent on the proposed increase in the required number of member-nominated trustees from one-third to 50%. We anticipate that further clauses are in the pipeline.

- **Cracking down on pension liberation** – to curb the number of members lured to transfer their benefits to bogus pension plans in return for cash, the Bill now incorporates new powers for the Pensions Regulator to deal with "pension liberation".

Finally, a number of technical changes affecting the operation of the PPF and the role of the Pensions Regulator in relation to European pensions issues have been introduced.